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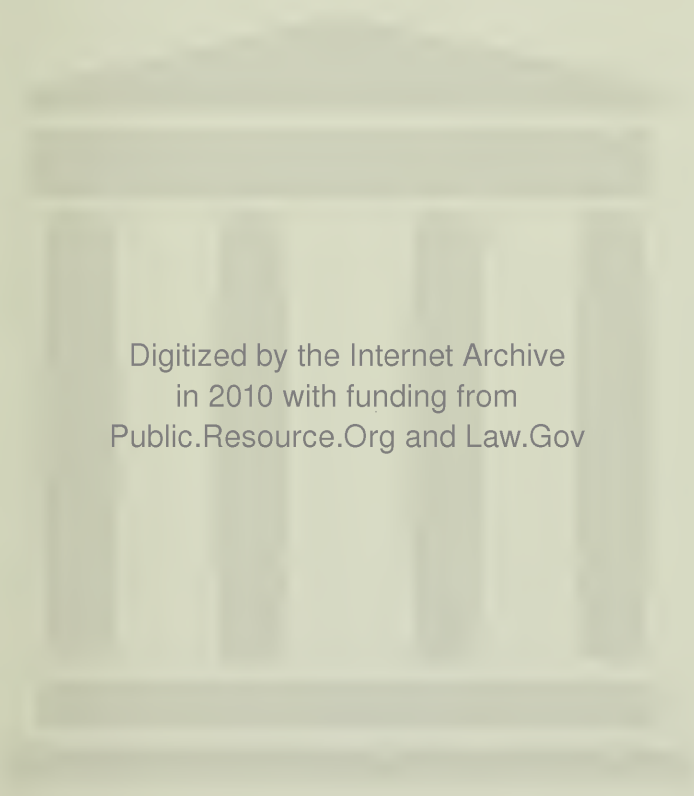
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2050
No. 15,651

United States Court of Appeals
For the Ninth Circuit

AMERICAN RADIATOR AND STANDARD
SANITARY CORPORATION, a Corpora-
tion,

Appellant,

vs.

L. L. FORBES and A. W. BODINE, Doing
Business as L. L. FORBES CONSTRUC-
TION COMPANY, and THE HOME IN-
DEMNITY COMPANY, a Corporation,

Appellees.

Appeal from the United States District Court
for the District of Arizona.

BRIEF FOR THE APPELLANT.

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FILED

OCT 23 1957

PAUL P. O'BRIEN, CLERK



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Home Indemnity Company is a corporation organized under the laws of the State of New York and is a citizen of that state. The defendant School District No. 205 is a body politic organized under the laws of the State of Arizona. The amount in controversy, exclusive of interest and costs, exceeds the sum of \$3,000. These jurisdictional facts were established in the District Court by the allegations of the amended complaint (R. 4), which were not denied and were found by the Trial Court to be true (R. 22).

The jurisdiction of the District Court rested upon diversity of citizenship. 28 U.S.C. § 1332.

The District Court, sitting without a jury, made formal findings of fact and conclusions of law and entered its judgment in favor of the defendants who are appellees and against the plaintiff. The judgment being final, the present appeal is predicated upon the provisions of 28 U.S.C. § 1291.

STATEMENT OF THE CASE.

This is an action brought by the appellant American Radiator and Standard Sanitary Corporation (whom we may call American Radiator from time to time throughout this brief) to recover from the several defendants the sum of \$10,493.13 as the unpaid balance of the purchase price of plumbing materials which it furnished for installation for the construction of classroom additions to Sunnyslope High School which is a part of the school system of the Glendale Union

High School District in Maricopa County, Arizona. The defendant members of the Board of Supervisors of the county and the School Board members, together with the District, were dismissed from the action upon their motion. No appeal was taken from this dismissal.

The action proceeded against the general contractors, L. L. Forbes and A. W. Bodine, doing business as L. L. Forbes Construction Company (to whom we shall refer in this brief either as Forbes or the Contractor) and The Home Indemnity Company (which we shall call the Bonding Company). There being no dispute between the parties with respect to any material issues of fact, except concerning the amount of damages, they entered into an agreed statement of facts setting forth such facts as were deemed necessary for a determination of the issue of liability of the remaining defendants and agreeing for the purpose of the cause that American Radiator had supplied some materials to the plumbing subcontractor which were incorporated in the classroom construction in question and that there was due and owing to American Radiator from the subcontractor a sum of money representing the purchase price of the materials and that American Radiator had never received payment from any person for such sum. The parties further agreed that there existed a disputed issue of fact concerning the description and purchase price of these materials (R. 14). By this stipulation the parties intended that the preliminary question of liability should first be decided by the court which would thus be relieved of the necessity of conducting an extended

accounting on the question of damages if the preliminary issue of liability were decided against the plaintiff.

Attached to the agreed statement of facts were the contract between Forbes and the School District and the contractor's bond issued by the Bonding Company. We have reproduced these two exhibits in the appendix to this brief.

The only other evidence before the court consisted of a notice to admit facts served by American Radiator and answered by Forbes (R. 18-19).

The parties submitted briefs and the court took the matter under advisement. On June 10, 1957, the court entered its order approving the defendants' findings of fact and conclusions of law and entering its judgment denying recovery to American Radiator against any of the defendants.

The facts material to the controversy are in substance as follows:

On September 30, 1954, Forbes, being the successful competitive bidder, entered into a contract with the School District for the construction of certain classroom additions to Sunnyslope High School. The contract was executed for the School District by the Board of Supervisors of Maricopa County acting as agent for the School District pursuant to the requirements of the Arizona statutes governing the letting of contracts for school construction. Under the Provisions of Article III of the contract, Forbes agreed to "provide and pay for all materials, labor, tools,

water, power and other items necessary to complete the work'' (App. iv). Simultaneous with the execution of the contract and in compliance with the provisions of § 10-610 of the 1939 Arizona Code Annotated, Forbes furnished to the School District a contract bond with the Bonding Company as surety (App. xiii).

Forbes awarded the subcontract for the plumbing work to W. M. Bachman. In an effort to perform the subcontract, Bachman in turn purchased plumbing materials and supplies from American Radiator to install in the job. In due course Bachman completed his subcontract with Forbes and was paid in full by Forbes.

The construction of the classrooms was completed and formal notice of completion was filed with the Board of Supervisors on July 16, 1955. Two days later, on July 18, American Radiator sent a registered letter to the School District, to Forbes, to the Bonding Company and to Bachman notifying each of them that there was due to American Radiator \$10,594.52 for plumbing materials which had been furnished for installation in the classrooms which were being built by Forbes for the School District. Each of the named addressees acknowledged having received the letter within five days. Although the precise amount of the sum of money which was due to American Radiator on July 16, 1955, is in dispute in this cause and remains for determination by the District Court, it is agreed that some sum of money was due to American Radiator on that date and that no payment has ever

been made to American Radiator by any person at any time on account of the balance due American Radiator.

Notwithstanding the registered letter from American Radiator putting the several addressees on notice that it had not been paid, the School District, through the Board of Supervisors, paid to Forbes the balance due on the general contract which had been retained for the 65-day statutory period after completion. This payment was made to Forbes, although Forbes had not (and in fact has never) furnished to the School District or the Board of Supervisors a satisfactory receipt from American Radiator for its bill for materials furnished by it for use in the construction of the classroom additions or a waiver of lien from American Radiator.

Since the facts relating to the issue of liability are not in dispute, the case presented to the District Court a pure and readily identifiable question of law. In essence, this question is whether, under the law of Arizona, a general contractor and his bonding company are liable to a supplier of materials to a subcontractor for school construction when

1. The general contractor has contracted in writing to provide and pay for all materials necessary to complete the work, and

2. The general contractor has accepted payment of the statutory retention fund without having furnished to the public authority any receipt or lien waiver evidencing payment for the materials, and

3. The general contractor has received prior actual notice that the material supplier has not been paid.

The District Court held that liability does not attach to the general contractor or his bonding company under these circumstances for the reason that neither the contractual undertaking of the general contractor nor the bond was in law a contract for the benefit of a materialman. It is our purpose by this brief to demonstrate that the law is otherwise.

SPECIFICATION OF ERRORS.

1. The District Court erred in not finding, in accordance with plaintiff's proposed additional findings of fact (R. 28), that the defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, never furnished to the Board of Supervisors of Maricopa County, Arizona, as agent for Glendale Union High School District, a satisfactory receipt from American Radiator and Standard Sanitary Corporation for its bill for materials furnished by it for use in the construction of classroom additions to Sunnyslope High School or a waiver of lien from American Radiator and Standard Sanitary Corporation, since the finding was supported by the record and was material to the determination of the issues of liability (R. 19).

2. The District Court erred in concluding, as it did in Conclusion of Law I (R. 25), that the contractual undertaking of the general contractor, the defendants

L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, under the contract marked "Exhibit A" to the agreed statement of facts is not a contract for the benefit of a third party and confers no rights upon the plaintiff to sue thereunder.

3. The District Court erred in concluding, as it did in Conclusion of Law II (R. 25), that the defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, did not undertake any obligation under the contract to pay for plumbing materials and supplies sold by the plaintiff to the plumbing contractor W. M. Bachman.

4. The District Court erred in concluding, as it did in Conclusion of Law III (R. 26), that the defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, did not undertake any obligation towards the plaintiff by furnishing and becoming a party to the bond on which The Home Indemnity Company was surety.

5. The District Court erred in concluding, as it did in Conclusion of Law IV (R. 26), that the bond furnished by defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, gave no rights to anyone other than the obligee.

6. The District Court erred in concluding, as it did in Conclusion of Law V (R. 26), that the bond furnished by the defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, is an indemnity bond containing no provisions for the benefit of the plaintiff or persons in the plaintiff's position.

7. The District Court erred in concluding, as it did in Conclusion of Law VI (R. 27), that the defendants L. L. Forbes and A. W. Bodine, dba L. L. Forbes Construction Company, complied with all the provisions of § 10-610, Arizona Code Annotated, 1939, as amended (1952 Supplement).

8. The District Court erred in concluding, as it did in Conclusion of Law VII (R. 27), that, construing the contract, the bond and the statutes of the state of Arizona together, there is no legal obligation imposed on any of the defendants who are appellees to pay for materials purchased by W. M. Bachman from the plaintiff for installation in the classroom additions to Sunnyslope High School and that plaintiff has no legal right to recover from those defendants who are appellees for such materials.

SUMMARY OF ARGUMENT.

I.

Forbes contracted with the School District to provide and pay for all materials necessary to complete the work. Although the named obligee in the contract was the Board of Supervisors acting as agent for the School District, the contract in law was for the benefit of laborers and materialmen, including American Radiator. The overwhelming weight of authority gives to a materialman, whether he supplies direct to the general contractor or to a subcontractor, the right to sue upon a contract of the character here involved.

II.

The contractor's bond was given in purported compliance with the provisions of the applicable Arizona statute governing contracts for the erection of schools and other public buildings. The statute required the contractor to furnish a bond in the amount of the contract conditioned upon the faithful performance of the contract. Under the familiar rule that a bond furnished in accordance with a statute is deemed to contain the minimum undertakings required by the statute, the bond furnished by the Bonding Company was in law conditioned upon the faithful performance of Forbes' contract, whether it expressly so stated or not. Efforts on the part of the Bonding Company and Forbes to limit the obligation of the bond to the indemnification of the School District and to deny to laborers and materialmen the right to sue on the bond were void to the extent that they conflicted with the statute and Forbes' contract. The contract being for the benefit of third parties, including American Radiator, the liability of the Bonding Company is coextensive with that of the contractor and American Radiator is entitled to sue and recover on the bond.

III.

The Arizona statute governing contracts for the erection of public buildings required the Board of Supervisors to retain 10% of the contract price as a guarantee of the faithful performance of the contract and to release it to Forbes only upon his furnishing satisfactory receipts for all labor and materials, and,

in any event, not prior to 65 days from completion of the contract. Since American Radiator never was paid and never gave to anyone a receipt for materials furnished by it for installation in the School buildings, Forbes could not and in fact did not furnish any satisfactory receipt to the Board of Supervisors for such materials. Notwithstanding this failure on Forbes' part to comply with the statute, the Supervisors released the 10% retention fund to Forbes. The Board of Supervisors paid and Forbes received the fund in violation of the statute. Since the fund was held as a guarantee of the faithful performance of the contract, including the undertaking by Forbes to pay for all materials necessary for the work, it was impressed with a constructive trust in favor of all persons, including American Radiator, who were entitled to the benefits of Forbes' contractual undertaking.

ARGUMENT.

I.

FORBES' CONTRACT WITH THE SCHOOL DISTRICT TO PAY FOR ALL MATERIALS IS A CONTRACT FOR THE BENEFIT OF MATERIALMEN, INCLUDING AMERICAN RADIATOR, UPON WHICH THEY MAY SUE AND RECOVER.

Article 1 of the agreement of September 30, 1954, between Forbes and the Board of Supervisors acting for the School District contains the following covenant (App. ii):

“The contractors shall furnish all of the material and perform all of the work. . . .”

Article 3 of the General Conditions which are expressly agreed to be a part of the contract provides as follows:

“Article 3. Materials, Appliances, Employes—Except as otherwise noted, the *Contractor shall provide and pay for all materials*, labor, tools, water, power and other items necessary to complete the work.

Unless otherwise specified, all materials shall be new, and both workmanship and materials shall be of good quality.

All workmen and sub-contractors shall be skilled in their trades.” (Emphasis supplied.)

Article 1 of the General Conditions makes it clear that the word “materials” as used in Article 3 was intended to embrace every kind of material necessary for the proper execution of the work. The pertinent language is as follows:

“The intent of these documents is to include all labor, materials, appliances and services of every kind necessary for the proper execution of the work, and the terms and conditions of payment therefor.”

It cannot be doubted that as between Forbes and the School District, he agreed to pay for materials of the character furnished by American Radiator to the plumbing subcontractor for incorporation in the Sunnyslope classroom additions. The only question presented in respect to the liability of Forbes under the contract is whether it is in law a third party beneficiary contract so that a materialman, such as

American Radiator, may sue and recover upon it, although it is not named as a party to the agreement. If the contract is for the benefit of third parties, including American Radiator, the judgment of the District Court in favor of Forbes must be reversed.

The jurisdiction of the court being predicated upon diversity of citizenship, the questions presented by this appeal must be decided with reference to the law of Arizona. If the courts of that state have not passed upon the issue definitively, it then becomes the task of this court to construct an Arizona rule from such pronouncements of its court as may provide a clue to the doctrine which would be adopted in Arizona if the question had been squarely presented. While we do not represent to this court that Arizona has expressly ruled on the issue at bar, we are persuaded by analogy that Arizona would rule for the materialman upon the facts presented by the record in this case.

The decision which most closely approximates the question now before the court is *Webb v. Crane Co.*, 52 Ariz. 299, 80 P. 2d 698. Crane Company furnished plumbing materials to a subcontractor to install in a state college building. Webb was the general contractor. After the work was completed, the plumbing subcontractor failed to pay Crane Company for the materials furnished by it. Crane sued Webb and his bonding company. One of the conditions of the bond filed by Webb was that the principal (Webb) pay all materialmen who supply materials, supplies or provisions for carrying on the work. Both the contract and the

bond named the State of Arizona as the sole obligee. Webb defended upon the ground that neither instrument was for the benefit of a third party materialman or gave him the right to sue thereon. The trial court found against both Webb and the bonding company. Only Webb appealed.

The Supreme Court of Arizona affirmed the judgment below. It based its reasoning primarily upon the proposition that since public buildings are not subject to liens, a remedy in lieu of the lien law was created by the requirement of a contractor's bond. The court expressly held that the bond was for the benefit of third parties, including the subcontractor's materialman, saying:

"We are clearly of the view that the performance bond given by appellant was for the protection of those who labored or furnished material on the addition to Taylor Hall, as well as the obligee mentioned therein, and was, therefore, a third party bond. *Knight & Jillson Co. v. Castle*, 172 Ind. 97, 87 N.E. 976, 27 L.R.A. (N.S.) 573, and note VIII, page 588. The following excerpt from the annotation in 77 A.L.R., p. 83, is a correct statement of law:

"'The right of laborers and materialmen to recover on a bond executed in connection with public works or improvements, where the bond contains a condition for their benefit and is intended for their protection, although the public body is the only obligee named therein, and there is no express provision that such third parties shall have any rights thereunder, is affirmed by the great weight of authority.'"

The only difference between *Webb v. Crane Co.* and the case at bar is that there the obligation to pay materialmen appeared in the bond, whereas here it appears in Forbes' contract, the faithful performance of which is guaranteed by the bond, as we shall later demonstrate. Let us consider whether this factual difference provides any basis for refusing to apply the rule of the *Webb* case. The holding of the *Webb* case is that a materialman to a subcontractor is a beneficiary of and may sue upon the undertaking of the general contractor as principal and his surety to pay all materialmen. The sole decision cited as support for the ruling of the Arizona court is *Knight & Jillson Co. v. Castle*, 172 Ind. 97, 87 N.E. 976. In that case Castle contracted with a church to construct a steam heating plant. His contract contained the following clause:

"The parties of the second part (Castle) agree to pay for all labor and materials used in said work when due. . . ."

This promise is in all respects identical to Forbes' promise to "provide and pay for all materials . . . necessary to complete the work."

Castle furnished a bond conditioned upon his faithful performance of the contract. Castle became insolvent and defaulted in his obligation to a materialman who sued Castle and his surety. Both defended upon the ground that the church was the sole obligee in the contract and bond and a materialman had no right to sue and recover upon either instrument. The Supreme Court of Indiana held that the agreement of the contractor to pay for all labor and materials

used in the work was made for the benefit of materialmen who had the right to sue and recover upon the contract and upon the bond which guaranteed its faithful performance. The rule adopted by the court is concisely set forth in the following excerpt from the decision:

“We have come to adopt two rules of construction with respect to undertakings of the character of the contract and bond sued on in this case, without, perhaps, noting carefully the distinctions in principle, as well as the distinctions between sureties and guarantors, as applied to the particular cases. One is that, where a contract is made primarily for the benefit of a third person, such agreement inures to the benefit of such person, even though the third person at the time had no knowledge of the agreement. The other is that *a contract to pay for labor or materials is a contract for the benefit of laborers and materialmen, and that upon default they may sue.*” (Emphasis supplied.)

Patently, the only essential differences between the *Knight & Jillson* case and the case at bar are (1) that Knight & Jillson Co. was a materialman to the general contractor, whereas American Radiator supplied a subcontractor, and (2) that the church was a private owner, whereas the School District is a public body.

In respect to the first difference, *Webb v. Crane* has resolved all doubts for Arizona by permitting a supplier of plumbing supplies to a subcontractor to recover as a third party beneficiary of the general contractor's bond. This conclusion is in accord with the

overwhelming weight of authority in other jurisdictions. The same question was before the Fourth Circuit Court of Appeals in *Standard Acc. Ins. Co. v. Simpson*, 64 F.2d 583. The court held both the contractor and his surety liable to a subcontractor's materialman, saying (at p. 589):

"Each of the bonds, signed by the contractor as well as the surety, guaranteed that the contractor would 'pay when and as due all lawful claims for labor performed or materials and supplies furnished for use in and about the construction of said highway or highway structures'; and we do not see how the letting of a part of the work to a subcontractor could be held to absolve the contractor or the surety from the obligation so undertaken. The public authorities were interested in providing that those who furnished labor or materials for the construction of the highways should be paid for them; the bonds were taken for the purpose of guaranteeing that this would be done; the contractor could not have obtained the contracts without giving such bonds; and we do not think that, after they have been given and the contracts thereby obtained, laborers and materialmen, for whose protection they were required, should go unpaid because the work has been let to a subcontractor, who has given an inadequate bond and who proves to be insolvent. This has been expressly decided by the Supreme Court of the United States in suits instituted under the Hurd Act (40 USCA § 270). *United States for Use of Hill v. American Surety Co.*, 200 U.S. 197, 26 S. Ct. 168, 50 L. Ed. 437; *Mankin v. U. S. to Use of Ludowici-Celadon Co.*, 215 U.S.

533, 30 S. Ct. 174, 54 L. Ed. 315. *And the same rule is supported by the overwhelming weight of authority in other jurisdictions. See exhaustive note in 70 A. L. R. 308 and cases there cited.*" (Emphasis supplied.)

The annotation in 70 A.L.R. has been supplemented in 111 A. L. R. 311.

The extension of protection to a subcontractor's materialman does not impose an unconscionable hardship upon the general contractor since he can readily protect himself by requiring his subcontractor to give a bond for the payment of laborers and materialmen. See *United States Use of Hill v. American Surety Company*, 200 U. S. 197, 50 L. Ed. 437, 26 S. Ct. 168; *City of Portland v. New England Casualty Co.*, 78 Ore. 195, 152 Pac. 253.

Actually, the decision of the District Court does not rest upon the distinction between materialmen to subcontractors and those furnishing directly to the general contractor. Conclusion of Law No. I holds unqualifiedly that the contract is not a contract for the benefit of a third party (R. 25). Presumably, this holding would similarly exclude from the benefits of the contract a materialman who supplied materials direct to Forbes. The cases supporting this narrow view are rare indeed.

The second distinction, namely that Forbes' contract was for a public building, actually favors recovery to American Radiator. A materialman's lien cannot be asserted against a public building. *Webb v. Crane*,

supra. A body politic and its officers are immune to liability for the non-payment of materialmen and laborers. As a consequence, the named obligee in a public contract and bond needs no protection. If, therefore, the undertaking of the contractor to pay for materials and labor is construed only as an obligation running to the public body, it is wholly meaningless and it is ordinarily not the policy of the law to construe agreements so that they will be wholly meaningless. Since the only class of persons who require protection are the materialmen and laborers, the contract will be construed to be intended for their benefit. This is the reasoning of the Supreme Court of Iowa in *Hipwell v. National Surety Co.*, 130 Iowa 656, 105 N. W. 318, 319:

“It is stipulated in the agreement ‘that the party of the second part further covenants and agrees to promptly pay for all labor and materials used in and about the building, and to hold and save the said first party harmless from and against all and every demand, or demands, of any nature or kind, for and on account of liens for labor and materials, or of the use of any patented invention, article or appliance included in the materials hereby agreed to be furnished under this contract.’ In no plainer language could the contractor have agreed ‘to promptly pay for all labor and materials used in and about the building.’ This cannot be regarded as merely introductory to what follows, as no liens for labor and material could in any event be asserted against the municipality, and such a construction would destroy the meaning of the entire paragraph, save the por-

tion relating to patented inventions and the like. Who then were to be paid? Manifestly those furnishing the labor and materials. The provision was for their benefit. No purpose other than this could have been served by the city, for in no event would it have been liable therefor. The evident object was to secure subcontractors to the end that knowing 'they were secured, would do better work and furnish better material than if they felt uncertain about their pay.' "

See also cases cited at 77 A.L.R. 141 and following.

The Supreme Court of Arizona has placed its reliance on the Indiana decision in *Knight & Jillson Co. v. Castle* in holding that a contract and bond for the payment of materialmen and laborers permits recovery by a materialman to a subcontractor. The decision of the Indiana court expressly holds that a contractual undertaking by a general contractor, in all material respects identical to the contract in the case at bar, is a promise to pay materialmen and laborers. When the Indiana and Arizona cases are laid side by side, they require the conclusion that the Supreme Court of Arizona would allow recovery to American Radiator against Forbes in this action.

II.

NOTWITHSTANDING ANY ATTEMPTS ON THE PART OF THE BONDING COMPANY TO RESTRICT ITS LIABILITY TO THE INDEMNIFICATION OF THE SCHOOL DISTRICT, THE BOND IS IN LAW A PERFORMANCE BOND IMPOSING LIABILITY ON THE BONDING COMPANY FOR ANY DEFAULT BY FORBES IN THE OBLIGATIONS OF THE CONTRACT.

The Bonding Company seeks to be relieved of liability by reliance upon two escape clauses which have been written into the bond (App. xiii). They are (1) that the condition of the bond is only that the Bonding Company shall indemnify the named obligee (the School District), and (2) that the instrument does not give to third parties the right to sue on it but undertakes expressly to deny to them that right.

Although neither question has been directly passed upon by the Supreme Court of Arizona, we believe that the tenor of its decisions, together with the better reasoned decisions in other jurisdictions, indicates that it would hold each of these escape clauses invalid under the circumstances here presented. At the outset, Arizona has expressly recognized the modern rule that a contract of suretyship made by a surety engaged in that business for profit will be construed most strongly against the surety and in favor of the person or persons for whose benefit the contract has been made. *Massachusetts Bonding Company v. Lentz*, 40 Ariz. 46, 9 P.2d 408.

The bond in this case was furnished in accordance with the provisions of § 10-610 of the 1939 Arizona Code as amended. The section has been reproduced in

full commencing at page xii of the appendix to this brief. It provides in part as follows:

“If a bid be accepted, said body or board (the Board of Supervisors) shall require the successful bidder to enter into a written contract for the erection and completion of said buildings and the furnishing thereof, and require from him a bond in the amount of the contract, *conditioned upon the faithful performance of the contract, such bond to be approved by the body or board.*”
(Parenthetical matter and emphasis supplied.)

The parties stipulated and the court found that the bond was a contract bond as required by § 10-610 (R. 15-23). It is a familiar rule that any undertaking of a contractual nature which purports to have been made in compliance with and for the purpose of qualifying under a provision of law is deemed to contain the minimum obligations established by that law and express provisions in the undertaking which conflict are regarded as being void. This rule has been expressly applied to surety bonds filed in purported compliance with the provisions of statutes relating to construction contracts for public works.

In *Baumann v. City of West Allis*, 187 Wis. 506, 204 N. W. 907, the surety sought to avoid liability on the ground that its bond was a performance bond only and the contract contained no express promise to pay materialmen. The Supreme Court of Wisconsin, first reviewing the requirements of its statutes concerning bonds for public works, said (p. 914 of 204 N. W.):

“It is the contention of appellants that the liability sought to be imposed by the statute does not

arise unless the provision required by the statute is actually inserted in the contract. If this construction is correct, then the relief which the Legislature attempted to afford subcontractors and materialmen is very much like sounding brass. The remedy which the Legislature intended to extend may, under such a construction, be defeated if the parties to the contract do not insert the prescribed provision, and whether the remedy is available to subcontractors and materialmen depends, not upon the law, but upon the parties to the contract. If this be the proper construction of the law, then the statute might just as well not have been passed, because such was the law before. Such a statute will be construed in the light of the conditions and circumstances which gave rise to the law, and to effectuate the purpose which the Legislature sought to accomplish. Having discovered that purpose, the law should be construed to give effect thereto. We entertain no doubt that it was the purpose of the Legislature to afford a remedy, in the nature of an action against the surety, to all subcontractors furnishing labor or material entering into the construction of public buildings and public works mentioned in the section of the statutes. This purpose may not be defeated by the voluntary act or by the oversight of the parties in failing to insert such a provision in the contract. The law imputes such provision to the contract whether written therein or not. The liability is one arising by virtue of the law, independent of the contract. Like the law providing for a standard fire insurance policy, it is both a law and a contract."

And in *City of Portland v. New England Casualty Co.*, *supra*, 152 Pac. at 254:

“The rights of the plaintiffs and the defendants are measured in accordance with the statutory bond required. In the execution of such an instrument the parties thereto are presumed to have had notice of and taken into consideration and understood the statute authorizing the same. The provisions of the act are practically made a part of the bond, just as though they were incorporated therein.”

See also *Guaranteed Gravel & S. Co. v. Aetna Casualty & S. Co.*, 174 Minn. 366, 219 N.W. 546.

As will be seen from these decisions the courts have forbidden the parties to change the law or limit the obligations which it imposes by private contract. By undertaking to furnish a bond, regardless of its form, the Bonding Company, as a matter of law, guaranteed the faithful performance of each of the covenants of the contract between Forbes and the School District. The Bonding Company in the capacity of surety contracted for liability precisely coextensive with the liability assumed by Forbes in the execution of the principal contract. If, as we have undertaken to demonstrate above, Forbes is liable to American Radiator under the construction contract, the Bonding Company must respond to the same liability if Forbes does not.

The second attempted escape is under the supposed protection of the clause which denies to any person other than the named obligee the right to institute pro-

ceedings and recover on the bond. Here again the better reasoned cases hold such an attempted limitation of remedies invalid. The theory upon which these decisions rest is that it is contrary to public policy to require a performance bond running to the benefit of laborers and materialmen and at the same time to deny to those persons judicial relief to enforce the right which has been granted to them. Some of the cases are collected in the annotation in 77 A.L.R. commencing at page 171. We think the following language from Judge Parker's decision in *Maryland Casualty Company v. Fowler*, 4 Cir., 31 F.2d 881, 63 A.L.R. 1375 commends itself to adoption:

"It is argued that the provision of the bond to the effect that no right of action shall accrue upon or by reason of it to any person other than the obligee, precludes the right of anyone else to recover thereunder. But, as the claims of laborers and materialmen were protected by the bond, this provision, insofar as it affects them, is void, because contrary to the public policy of the state as expressed in § 2445 of the Consolidated Statutes."

The Supreme Court of Iowa took a more pragmatic approach in *Hipwell v. National Surety Co.*, *supra* (105 N.W. at 320):

"It is contended, however, that, even if this paragraph be so construed, all liability to subcontractors is obviated by a subsequent provision that 'it is the express condition of this contract that no member of said committee, or other person, whose name is not at this time disclosed, shall be admitted to any share of this contract, or to any

benefit to arise therefrom; and it is further covenanted and agreed that this contract shall not be assigned.' That is, under the construction contended for the parties, after specifically agreeing that payment shall be promptly made for labor and materials, they then stipulated that none other than those named shall derive any benefit therefrom. It seems all but inconceivable that after recognizing that labor and materials must be bought by the contractor, and obligating him to promptly pay therefor, that this paragraph was intended to exclude those furnishing them from 'any share of this contract or to any benefit arising therefrom.' Just how such a feat, paying without conferring a benefit, may be performed, is not explained."

See also the supplemental annotation in 118 A.L.R. at page 86 and following.

One other defense which was asserted by the Bonding Company but which was not expressly made the subject of a finding or conclusion by the District Court is the provision of Paragraph Sixth of the bond requiring suit to be brought thereon within six months after the completion of the contract. Attempts to establish limitations other than the applicable Statute of Limitations are prohibited by the Arizona Insurance Code, A. R. S. § 20-1115, and the decision of the state Supreme Court in *Massachusetts Bonding Company v. Lentz*, *supra*.

It is, of course, true that the bond does not contain any express agreement to pay the claims of laborers

and materialmen. The detailed obligations of the general contractor are set forth in his written contract which in this case must be construed as an agreement to pay a materialman supplying materials to a subcontractor. It is, however, of no consequence whether the undertaking to pay materialmen is found in the bond or is found only in the contract, the performance of which the bond guarantees. The contract and bond must be read together to determine the extent of the surety's liability. *Hartford Accident and Indemnity Company v. Board of Education*, 4 Cir., 15 F.2d 317; *First National Bank v. Caples*, 5 Cir., 17 F.2d 87. See cases collected in 77 A.L.R. at page 96 where the annotator says:

“And if a public contractor's bond conditioned for the faithful performance of the contract, and the contract and specifications or other papers made a part of the contract, fairly construed together, show an obligation on the part of the contractor to pay persons furnishing materials, the materialman may sue and recover on the bond.”

Here, again, no valid distinction can be made between suppliers to the general contractor and those who furnish materials to a subcontractor. The cases which we have cited in respect to Forbes' liability apply without discrimination to both the principal and the surety whose liability is necessarily coextensive with that of the contractor. See annotations in 70 A.L.R. 308 and 111 A.L.R. 311. Indeed, the District Court's decision does not purport to rest upon any such supposed distinction. Conclusions of Law

Nos. IV and V hold that the Bonding Company, with complete disregard for the statute, has lawfully limited its undertaking to that of indemnification of the named obligee, and no one else, not even a direct supplier to Forbes, may invoke the protection of the bond (R. 26).

In summary, it is our position that the bond, being furnished in purported compliance with the statute, is conditioned on the faithful performance of the contract by Forbes, that Forbes agreed to pay all materialmen, including suppliers to his subcontractors, that any attempts on the part of the Bonding Company to deny to materialmen the right to sue on the bond are void and that the Bonding Company is liable to the same extent as Forbes.

III.

BY ACCEPTING THE FINAL RETENTION FUND WITHOUT FURNISHING TO THE SCHOOL DISTRICT A SATISFACTORY RECEIPT FOR THE MATERIALS SUPPLIED BY AMERICAN RADIATOR, FORBES BECAME A CONSTRUCTIVE TRUSTEE OF THE FUND FOR THE BENEFIT OF AMERICAN RADIATOR.

Section 10-610 (App. xii) contains certain specific restraints on the final release of the balance of the contract price to the contractor after completion of the building. They are:

1. That 10% of all estimates shall be retained by the Board of Supervisors "as guarantee of the complete performance of the contract", and

2. That this 10% retention fund shall be paid to the contractor on the happening of both of the following events:

- (a) That 65 days have elapsed after completion of the contract.
- (b) That the contractor has duly furnished to the Board of Supervisors "satisfactory receipts for all labor and material bills and waivers of liens from any and all persons holding claims against the work".

The record discloses that the 10% retention fund was paid by the Board of Supervisors to Forbes notwithstanding the following circumstances which existed at the time of payment:

- 1. Forbes had not completely performed the contract, in that he had not paid for all materials required for the job.
- 2. Prior to the expiration of 65 days from the completion of the building, Forbes and the School District had received written notice that American Radiator had not been paid.
- 3. Neither before the release of the retention fund nor at any time thereafter did Forbes ever furnish to the Board of Supervisors or the School District any satisfactory receipt from American Radiator for the material supplied by it nor a waiver of lien.

As we have observed in the first part of this argument, (p. 19) neither the Board of Supervisors nor

the School District is liable for unpaid bills for materials furnished for the construction work. The public buildings and the land on which they stand are, of course, immune to materialmen's liens. In consequence, it is apparent that the requirement that 10% of the contract price be retained until the contractor has furnished receipts for material and waivers of liens could not have been designed to protect the public bodies or the public property. It is equally apparent that the only persons who might be the beneficiaries of the statutory restraints on the release of the retention fund are the persons who perform the labor and furnish the materials.

In his Admission of Facts, Forbes admitted that he never furnished to the Supervisors a receipt from American Radiator but added that it was not necessary for him to furnish such receipts or waivers of lien from American Radiator, inasmuch as he did in fact furnish to the Supervisors receipts from the plumbing subcontractor to whom American Radiator furnished the plumbing materials (R. 19). This is, of course, a distortion of the language of the statute. A receipt for a material bill signed by any person other than the vendor of the material is not "satisfactory". The only kind of a receipt which is "satisfactory" is one which constitutes evidence of payment to that person who is entitled to receive payment. Since payment to the plumbing subcontractor does not constitute satisfaction of the claim of American Radiator, a receipt signed by the subcontractor is no receipt at all.

We think that further evidence of the intention of the legislature to insist upon receipts from those persons entitled to payment is to be found in the alternate requirement that the contractor shall provide waivers of liens from any and all persons holding claims against the work. Clearly, a subcontractor could not waive a lien which a materialman would be entitled to assert if the public structure were subject to such liens. Clearly, a waiver purported to be signed by a subcontractor could not prohibit his materialman from successfully filing and foreclosing a lien for materials actually incorporated in the structure. We think that the statute read as a whole compels the interpretation that a Board of Supervisors may not lawfully pay nor may the general contractor lawfully receive the final 10% of the contract unless the general contractor has furnished to the Board a satisfactory receipt executed by every person who would be in a position to perfect a laborer's or materialman's lien if the property were not in public ownership. Any other construction would strip laborers and materialmen of the minimum protection available to them on public jobs.

Additionally, the statute requires that the retention fund be held as a "guarantee of the complete performance of the contract. . . ." As we have seen, the contract required Forbes to pay for all labor and materials. Until he had discharged that obligation, together with all the other obligations of the contract, the retention fund stood as a guarantee against his default and could not lawfully be paid to him.

The conclusion is therefore inescapable that when the Board of Supervisors as agent for the School District paid the final retention fund to Forbes, it paid and Forbes accepted the fund in violation of express statutory restraints.

It is, of course, true that the Supervisors, the Trustees of the School District and the District itself were joined as defendants in this action and that the court, upon their motion, dismissed the complaint as to them. Appellees will contend that this dismissal was a ruling by the District Court that the payment of the retention fund was not in violation of any of the provisions of § 10-610. We took no appeal from the order of dismissal and we have no quarrel with it. It is fully justified upon the doctrine that an action will not lie against the body politic or the members of its governing board for acts in violation of express statutory inhibitions unless the right to maintain such an action is expressly granted by statute. Precisely in point is the following quotation from 44 Corpus Juris at p. 414 upon which the County Attorney relied in urging his motion to dismiss as to the Supervisors and School authorities:

“While a person who has . . . furnished materials to . . . a contractor for a municipal improvement may in a proper case recover a personal judgment against the contractor, he has no claim or right of action against the municipality unless the case is brought within an applicable statute imposing liability. . . .”

Surely the order of dismissal could not, in the face of the statutory language, have constituted a finding

by the trial Court that the contractor had complied with all of the provisions of the law. It simply meant that the departure from the statutory restraints did not give rise to a cause of action against the public authorities.

Clearly, Forbes took the final 10% in violation of the law. Clearly, he held it as a guarantee of the complete performance of his contract. The fund came into his hands impressed with a constructive trust for the benefit of those persons whom the legislature intended to protect. This is in substance the conclusion which was reached by the Court of Appeals of Colorado in *Western Lumber & Pole Co. v. City of Golden*, 23 Colo. App. 461, 130 Pac. 1027. The Colorado statute contained a provision requiring a City Council to retain funds for the payment of claims of materialmen and laborers. In violation of this restraint the City Council of the City of Golden released the retention fund when there were unsatisfied materialmen's claims. The court held that by the statute the city was made the agent or trustee for the unpaid claimant and that the fund in the hands of the city was impressed with a trust in his favor. The court said (at p. 1029 of 130 Pac.):

“By section 5406, in the most unequivocal language, the trustee created by the statute, namely, the city in this case, is enjoined to withhold the payment of money due the contractor, and the purpose for which it is to be withheld is clearly expressed: ‘To satisfy the claim of laborers,’ etc. *Section 5407, in language requiring no interpretation, positively forbids payment by the city to*

the contractor until he shall have done the things imposed upon him by the statute; and this no matter what the terms of the contract between the city and the contractor may be." (Emphasis supplied.)

Under the provisions of § 10-610 the Board of Supervisors held the retention fund as a guarantee for the performance of the contract. Article 3 of the General Conditions of the contract required the contractor to pay for all materials. The legal effect of the statute was that the fund was held by the Board of Supervisors as a guarantee for the payment of material bills, including the bill presented by American Radiator. In consequence, the Board of Supervisors held the fund as trustee for unpaid materialmen, including American Radiator.

Surely, if the fund was impressed with a trust while it was in the hands of the Board of Supervisors, the trust followed the fund into the hands of the contractor who received it in violation of the law.

CONCLUSION.

The judgment of the District Court has in practical consequence effectively frustrated the aims and purposes of the Arizona statute. It has thrown upon the laborer and the materialman the risk of the insolvency of the subcontractor. Inevitably, if such materialmen and laborers are deprived of any protection from the statutory undertakings of the general contractor and

his surety, their only recourse is to hedge anticipated losses either by increasing the price of their services and materials or stinting on quality. The Supreme Court of the United States sees this as a matter of public concern.

“The public is concerned not merely because laborers and materialmen (being without the benefit of a mechanics’ lien in the case of public buildings) would otherwise be subject to great losses at the hands of insolvent or dishonest contractors, but also because the security afforded by the bond has a substantial tendency to lower the prices at which labor and material will be furnished, because of the assurance that the claims will be paid.” *Equitable Surety Co. v. United States*, 234 U.S. 448, 58 L. Ed. 1394, 34 S. Ct. 803, 805.

The judgment of the District Court should be reversed and the cause remanded with instructions to enter judgment in favor of the plaintiff upon a proper showing of the value of the materials furnished.

Dated, Phoenix, Arizona,

October 18, 1957.

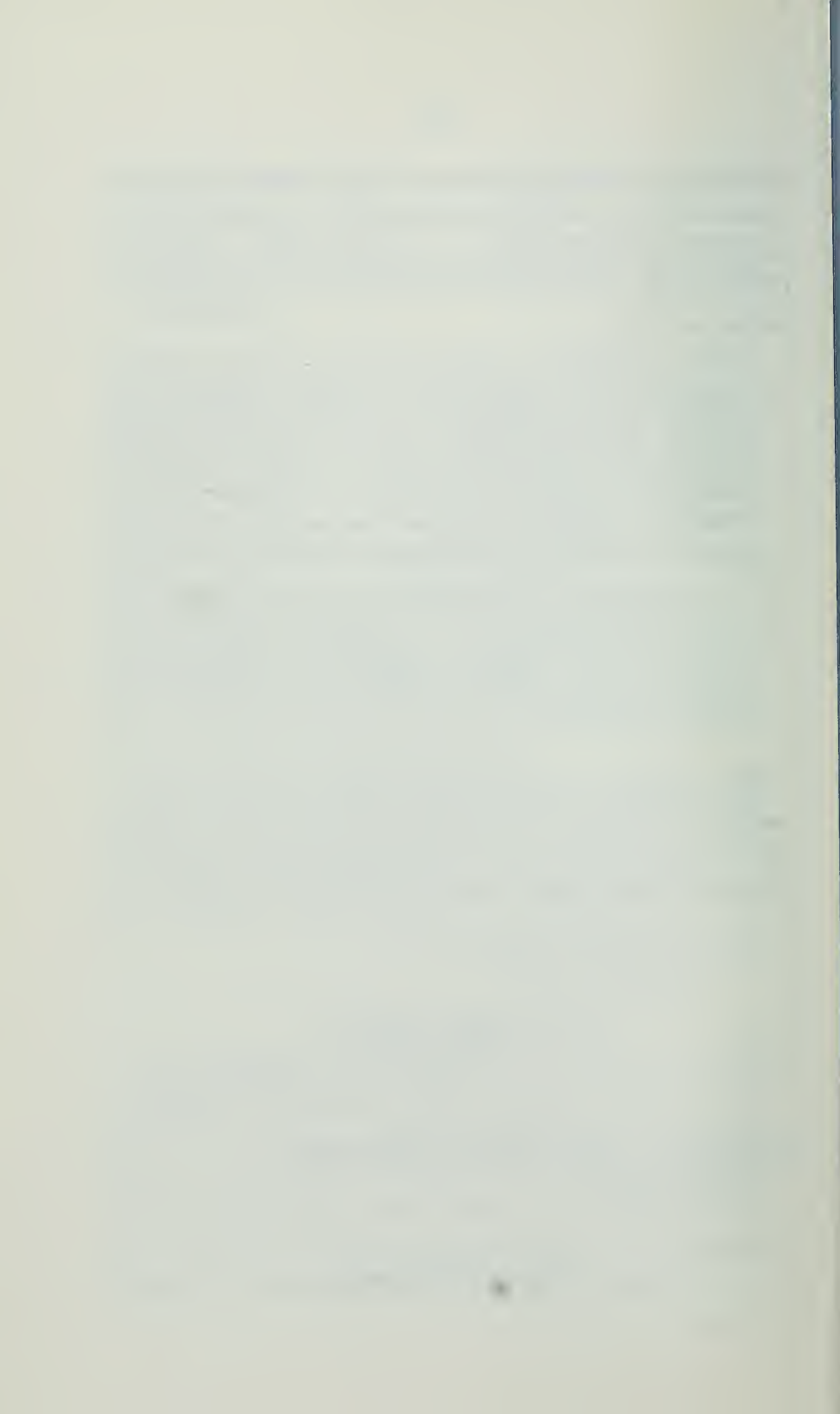
Respectfully submitted,

PHILIP E. VON AMMON,

Attorney for Appellant.

FENNEMORE, CRAIG, ALLEN & MCCLENNEN,
Of Counsel.

(Appendix Follows.)



Appendix.



Appendix

THE A.I.A. SHORT FORM FOR SMALL CONSTRUCTION CONTRACTS

AGREEMENT AND GENERAL CONDITIONS BETWEEN CONTRACTOR AND OWNER

ISSUED BY THE AMERICAN INSTITUTE OF ARCHITECTS FOR USE ONLY WHEN THE PROPOSED WORK IS SIMPLE IN CHARACTER, SMALL IN COST, AND WHEN A STIPULATED SUM FORMS THE BASIS OF PAYMENT, FOR OTHER CONTRACTS THE INSTITUTE ISSUES THE STANDARD FORM OF AGREEMENT BETWEEN CONTRACTOR AND OWNER FOR CONSTRUCTION OF BUILDINGS AND THE STANDARD GENERAL CONDITIONS IN CONNECTION THEREWITH FOR USE WHEN A STIPULATED SUM FORMS THE BASIS FOR PAYMENT.

SIXTH EDITION, COPYRIGHT, 1936-1951 BY THE AMERICAN INSTITUTE OF ARCHITECTS, THE OCTAGON, WASHINGTON, D. C.

THIS AGREEMENT made the *30th* day of *September* in the year Nineteen Hundred and *fifty-four*, by and between *L. L. FORBES CONSTRUCTION COMPANY, A Partnership*, hereinafter called the

Contractor, and *BOARD OF SUPERVISORS OF MARICOPA COUNTY, ARIZONA, ACTING FOR GLENDALE UNION HIGH SCHOOL DISTRICT* hereinafter called the Owner.

WITNESSETH, That the Contractor and the Owner for the consideration hereinafter named agree as follows:

Article 1. Scope of the Work—The Contractor shall furnish all of the material and perform all of the work for *Gymnasium, Classroom Additions and Bus Garage* (Caption indicating the portion or portions of work covered) as shown on the drawings and described in the specifications entitled

A Gymnasium Building for Sunnyslope High School, Glendale Union High School District, Maricopa County, Sunnyslope, Arizona, by Edward L. Varney Architects, Inc., and Classroom Additions to Sunnyslope High School, by John Sing Tang.

prepared by *EDWARD L. VARNEY ARCHITECTS, INC.-JOHN SING TANG* Architects all in accordance with the terms of the contract documents.

Article 2. Time of Completion—The work shall be substantially completed *within 180 days after the date of the contract.*

Article 3. Contract Sum—The Owner shall pay the Contractor for the performance of the contract subject to the additions and deductions provided therein in

current funds, the sum of *TWO HUNDRED FIFTY-SIX THOUSAND SEVEN HUNDRED EIGHT & NO/100 dollars.* (\$256,708.00)

Article 4. Progress Payments—The Owner shall make payments on account of the contract, upon requisition by the Contractor, as follows:

On the first of every month, the Contractor shall be paid the amount of work in place, less the aggregate of prior payments, and less 10% which amount will be retained for final payment. These payments shall be made on the certificates of the Architects only.

Article 5. Acceptance and Final Payment—Final payment shall be due 10 days after completion of the work, provided the contract be then fully performed, subject to the provisions of Article 16 of the General Conditions.

Article 6. Contract Documents—Contract documents are as noted in Article 1 of the General Conditions. The following is an enumeration of the drawings and specifications:

Drawings:	GA1, 2, 3, 4, 5, GS1, 2, GE1	By Edward
Specifications:	Sections I, II, III, Addendum # 1	L. Varney Architect, Inc.
Drawings:	A1 thru A11, S1, 2,3; M1, 2, E1, E2, P1, 2, 3	By John
Specifications:	73 pages, Addenda 1, 2, 3 and 3 Addenda Drawing Sheets	Sing Tang

All as applicable to Base Bid 3 of the Bid Form.

GENERAL CONDITIONS

Article 1. Contract Documents—The contract includes the Agreement and its General Conditions, the Drawings, and the Specifications. Two or more copies of each, as required, shall be signed by both parties and one signed copy of each retained by each party.

The intent of these documents is to include all labor, materials, appliances and services of every kind necessary for the proper execution of the work, and the terms and conditions of payment therefor.

The documents are to be considered as one, and whatever is called for by any one of the documents shall be as binding as if called for by all.

Article 2. Samples—The Contractor shall furnish for approval all samples as directed. The work shall be in accordance with approved samples.

Article 3. Materials, Appliances, Employes—Except as otherwise noted, the Contractor shall provide and pay for all materials, labor, tools, water, power and other items necessary to complete the work.

Unless otherwise specified, all materials shall be new, and both workmanship and materials shall be of good quality.

All workmen and sub-contractors shall be skilled in their trades.

Article 4. Royalties and Patents—The Contractor shall pay all royalties and license fees. He shall defend all suits or claims for infringement of any patent

rights and shall save the Owner harmless from loss on account thereof.

Article 5. Surveys, Permits, and Regulations—The Owner shall furnish all surveys unless otherwise specified. Permits and licenses of a temporary nature necessary for the prosecution of the work shall be secured and paid for by the Contractor. Permits, licenses and easements for permanent structures or permanent changes in existing facilities shall be secured and paid for by the Owner, unless otherwise specified. The Contractor shall comply with all laws and regulations bearing on the conduct of the work and shall notify the Owner if the drawings and specifications are at variance therewith.

Article 6. Protection of Work, Property, and Persons—The Contractor shall adequately protect the work, adjacent property and the public and shall be responsible for any damage or injury due to his act or neglect.

Article 7. Inspection of Work—The Contractor shall permit and facilitate inspection of the work by the Owner and his agents and public authorities at all times.

Article 8. Changes in the Work—The Owner may order changes in the work, the Contract Sum being adjusted accordingly. All such orders and adjustments shall be in writing. Claims by the Contractor for extra cost must be made in writing before executing the work involved.

Article 9. Correction of Work—The Contractor shall re-execute any work that fails to conform to the requirements of the contract and that appears during the progress of the work, and shall remedy any defects due to faulty materials or workmanship which appear within a period of one year from the date of completion of the contract. The provisions of this article apply to work done by subcontractors as well as to work done by employes of the Contractor.

Article 10. Owner's Right to Terminate the Contract—Should the Contractor neglect to prosecute the work properly, or fail to perform any provision of the contract, the Owner, after seven days' written notice to the Contractor, may, without prejudice to any other remedy he may have, make good the deficiencies and may deduct the cost thereof from the payment then or thereafter due the Contractor or, at his option, may terminate the contract and take possession of all materials, tools, and appliances and finish the work by such means as he sees fit, and if the unpaid balance of the contract price exceeds the expense of finishing the work, such excess shall be paid to the Contractor, but if such expense exceeds such unpaid balance, the Contractor shall pay the difference to the Owner.

Article 11. Contractor's Right to Terminate Contract—Should the work be stopped by any public authority for a period of thirty days or more, through no fault of the Contractor, or should the work be stopped through act or neglect of the Owner for a period of seven days, or should the Owner fail to

pay the Contractor any payment within seven days after it is due, then the Contractor upon seven days' written notice to the Owner, may stop work or terminate the contract and recover from the Owner payment for all work executed and any loss sustained and reasonable profit and damages.

Article 12. Payments—Payments shall be made as provided in the Agreement. The making and acceptance of the final payment shall constitute a waiver of all claims by the Owner, other than those arising from unsettled liens or from faulty work appearing thereafter, as provided for in Article 9, and of all claims by the Contractor except any previously made and still unsettled. Payments otherwise due may be withheld on account of defective work not remedied, liens filed, damage by the Contractor to others not adjusted, or failure to make payments properly to subcontractors or for material or labor.

Article 13. Contractor's Liability Insurance—The Contractor shall maintain such insurance as will protect him from claims under workmen's compensation acts and from claims for damages because of bodily injury, including death, which may arise from and during operations under this contract, whether such operations be by himself or by any subcontractor or anyone directly or indirectly employed by either of them. This insurance shall be written for not less than any limits of liability specified as part of this contract. This insurance need not cover any liability imposed by Article 6 of the General Conditions. Certificates of such insurance shall be filed with the Owner if he so require.

Article 14. Owner's Liability Insurance—The Owner shall be responsible for and at his option may maintain such insurance as will protect him from his contingent liability to others for damages because of bodily injury, including death, which may arise from operations under this contract, and any other liability for damages which the Contractor is required to insure under any provision of this contract.

Article 15. Fire Insurance—The Owner shall effect and maintain fire insurance upon the entire structure on which the work of this contract is to be done to one hundred per cent of the insurable value thereof, including items of labor and materials connected therewith whether in or adjacent to the structure insured, materials in place or to be used as part of the permanent construction including surplus materials, shanties, protective fences, bridges, or temporary structures, miscellaneous materials and supplies incident to the work; and such scaffoldings, stagings, towers, forms, and equipment as are not owned or rented by the contractor, the cost of which is included in the cost of the work. Exclusions: This insurance does not cover any tools owned by mechanics, any tools, equipment, scaffoldings, stagings, towers, and forms owned or rented by the Contractor, the capital value of which is not included in the cost of the work, or any cook shanties, bunk houses or other structures erected for housing the workmen. The loss, if any, is to be made adjustable with and payable to the Owner as Trustee for the insureds as their interests may appear, except in such cases as may require payment of

all or a proportion of said insurance to be made to a mortgagee as his interests may appear.

The Contractor and all sub-contractors shall be named or designated in such capacity as insured jointly with the Owner in all policies, all of which shall be open to the Contractor's inspection. Certificates of such insurance shall be filed with the Contractor if he so requires. If the Owner fails to effect or maintain insurance as above and so notifies the Contractor, the Contractor may insure his own interest and that of the sub-contractor and charge the cost thereof to the Owner. If the Contractor is damaged by failure of the Owner to maintain such insurance or to so notify the Contractor, he may recover as stipulated in the contract for recovery of damages. If extended coverage or other special insurance not herein provided for is required by the Contractor, the Owner shall effect such insurance at the Contractor's expense by appropriate riders to his fire insurance policy.

If required in writing by any party in interest, the Owner as Trustee shall, upon the occurrence of loss, give bond for the proper performance of his duties. He shall deposit any money received from insurance in an account separate from all his other funds and he shall distribute it in accordance with such agreement as the parties in interest may reach, or under an award of arbitrators appointed, one by the Owner, another by joint action of the other parties in interest, all other procedure being as provided elsewhere in the contract for Arbitration. If after loss no special agree-

ment is made, replacement of injured work shall be ordered and executed as provided for changes in the work.

The Trustee shall have power to adjust and settle any loss with the insurers unless one of the Contractors interested shall object in writing within three working days of the occurrence of loss, and thereupon arbitrators shall be chosen as above. The Trustee shall in that case make settlement with the insurers in accordance with the directions of such arbitrators, who shall also, if distribution by arbitration is required, direct such distribution.

Article 16. Liens—The final payment shall not be due until the Contractor has delivered to the Owner a complete release of all liens arising out of this contract, or receipts in full covering all labor and materials for which a lien could be filed, or a bond satisfactory to the Owner indemnifying him against any lien.

Article 17. Separate Contracts—The Owner has the right to let other contracts in connection with the work and the Contractor shall properly cooperate with any such other contractors.

Article 18. The Architect's Status—The Architect shall have general supervision of the work. He has authority to stop the work if necessary to insure its proper execution. He shall certify to the Owner when payments under the contract are due and the amounts to be paid. He shall make decisions on all claims of the Owner or Contractor. All his decisions are subject to arbitration.

Article 19. Arbitration—Any disagreement arising out of this contract or from the breach thereof shall be submitted to arbitration, and judgment upon the award rendered may be entered in the court of the forum, state or federal, having jurisdiction. It is mutually agreed that the decision of the arbitrators shall be a condition precedent to any right of legal action that either party may have against the other. The arbitration shall be held under the Standard Form of Arbitration Procedure of The American Institute of Architects or under the Rules of the American Arbitration Association.

Article 20. Cleaning Up—The Contractor shall keep the premises free from accumulation of waste material and rubbish and at the completion of the work he shall remove from the premises all rubbish, implements and surplus materials and leave the building broom-clean. In Witness Whereof the parties hereto executed this Agreement, the day and year first above written.

L. L. Forbes Construction Company
Contractor A. W. Bodine, Partner
Board of Supervisors of Maricopa
County, Arizona, acting for Glen-
dale Union High School District
Owner James G. Harth, Chairman
Attest:—4—

Marguerite Trujillo

Actg. Clerk

Section 10-610, Arizona Code Annotated—1939.
Erection of buildings for which bonds voted—Method of payment—If such bonds are issued for the purpose of erecting and furnishing any public building, the board of supervisors, for a county or school district, and the governing body of a city, town, or other municipal corporation, shall adopt plans and specifications for such building and as soon as practicable thereafter, advertise for bids for the erection and furnishing of said building, stating a day and hour, not less than forty [40] days from the date of such notice, when said bids shall be received and opened. The governing body or board shall award the contract to the lowest and most responsible bidder, but any and all bids submitted may be rejected. If a bid be accepted, said body or board shall require the successful bidder to enter into a written contract for the erection and completion of said buildings and the furnishing thereof, and require from him a bond in the amount of the contract, conditioned upon the faithful performance of the contract, such bond to be approved by the body or board. Such body or board may agree to pay the contractor in semi-monthly or monthly payments as may be authorized by law or by mutual agreement, to be due and paid to the contractor upon a basis of ninety [90] per cent of the value of the work actually performed as estimated by the architect or superintendent up to and including the 15th or last day of each calendar month; ten [10] per cent of all estimates shall be retained by the agent as guarantee of the complete performance of the contract, to be paid to the

contractor within sixty-five [65] days after completion, or filing of notice of completion, or [of] the contract, provided the contractor has duly furnished the agent satisfactory receipts for all labor and material bills and waivers of liens from any and all persons holding claims against the work. Such contract shall be signed by the agent and the contractor. If it is necessary to purchase a building site, the call for the election shall state the amount to be expended therefor.

The Home Indemnity Company
Home Office—New York

CONTRACT BOND

Bond No. N 197022

Know All Men By These Presents:

That L. L. Forbes Construction Company, A Partnership of Phoenix, Arizona, (hereinafter called the Principal), and The Home Indemnity Company (hereinafter called the Surety), are held and firmly bound unto Board of Supervisors of Maricopa County, Arizona acting for Glendale Union High School District of Maricopa County, Arizona (hereinafter called the Obligee), in the sum of Two Hundred Fifty-Six Thousand Seven Hundred Eight and 00/100 Dollars (\$256,708.00), for the payment whereof said Principal and Surety Bind themselves firmly by these presents.

Whereas, The Principal has entered into a written contract dated the 30th day of September, 1954, with the Obligee for a gymnasium building for Sunnyslope High School, Glendale Union High School District,

Maricopa County, Sunnyslope, Arizona by Edward L. Varney Architects, Inc., and classroom additions to Sunnyslope High School by John Sing Tang, which contract, subject to the conditions and provisions herein set forth, is made a part hereof for the purpose of explaining this obligation:

Now, Therefore, The condition of this obligation is such that if the Principal shall indemnify the Obligee against loss or damage directly caused by the failure of the Principal to faithfully perform said contract, then this obligation shall be void; otherwise to remain in full force and effect.

Provided, however, and upon the *Express Conditions* the performance of each of which shall be a condition precedent to any right of recovery hereon:

FIRST: That in the event of any default on the part of the Principal, a written statement of the particular facts showing such default and the date thereof shall be delivered to the Surety, by registered mail, at its office in New York, New York, promptly and in any event within ten (10) days after the Obligee or his representative, or the Architect, if any, shall learn of such default; and if the Principal abandons said contract or is lawfully compelled by reason of a default to cease operations thereunder the Surety shall have the right within thirty (30) days after the receipt of notice from the Obligee that the Principal has ceased operations under the contract to proceed, or procure others to proceed, with the performance of such a contract as if no default or abandonment had

occurred, and in such event all moneys or property due or to become due under said contract shall as the same become due and payable under the terms of the contract to be paid to the Surety; but if the Obligee completes or relets the contract, all moneys or property provided by the contract to be paid to the Principal, had the Principal faithfully performed said contract, shall be credited upon any claim against the Surety, and the surplus, if any, applied as the Surety may direct.

SECOND: That the Obligee shall faithfully perform all the terms, covenants and conditions of such contract on the part of the Obligee to be performed; and shall also retain that proportion, if any, which such contract specifies the Obligee shall or may retain of the value of all work performed or materials furnished in the prosecution of such contract (not less however, in any event, than ten per centum of such value), until the complete performance by the Principal of all the terms, covenants and conditions of said contract on the Principal's part to be performed.

THIRD: That the plans and specifications mentioned in said contract are not in any respect defective, and are and at all times will be kept adequate for the complete performance of such contract, and that no change shall be made in such plans and specifications which shall increase the amount to be paid to the Principal more than ten per centum of the penalty of this instrument, without the written consent of the Surety.

FOURTH: That the Surety shall not be liable for any loss or damage resulting from so-called strikes or labor difficulties, or from mobs, riots, fire, the elements, civil commotion, or acts of God, or the public enemies, or for the repair or reconstruction of any work or materials damaged or destroyed by any such causes; nor for loss or damages from injury to or death of persons; nor for patent infringement; nor for non-performance of any guarantees of the efficiency or wearing qualities of any work done or materials furnished or the maintenance thereof or repairs thereto; nor for the furnishing of any bond or obligation other than this instrument; nor for damages caused by delay in finishing such contract in excess of ten per centum of the penalty of this bond.

FIFTH: That no right of action shall accrue upon or by reason hereof to or for the use of anyone other than the Obligee herein named; that the obligation of the Surety is, and shall be construed strictly as, one of suretyship only; that this bond shall be executed by the Principal before delivery, and shall not, nor shall any interest therein, or right of action thereon, be assigned without the prior consent in writing of the Surety, over the signature of its president or vice-president, attested by its secretary or assistant secretary; nor shall any of the conditions or provisions contained herein be deemed waived or altered by the Surety unless the written consent to such waivers or alteration be duly executed by its president or vice-president and attested as aforesaid.

SIXTH: That no action, suit or proceeding shall be had or maintained against the Surety on this instrument unless the same be brought or instituted and process served upon the Surety within six months after the completion of the said contract and in any event within twelve (12) months from the date fixed in said contract for completion, and if no time for completion is specified in said contract, after eighteen months from the date of this bond; that the Principal shall be made a party to any such suit or action, and be served with process commencing the same if the Principal can with reasonable diligence be found; and that no judgment shall be rendered against the Surety in excess of the penalty of this bond. If any limitation set forth in this condition is prohibited by the statutes of the state in which this bond is issued, the said limitation shall be considered to be amended to agree with the minimum period of limitation permitted by such statutes.

Signed and Sealed this 30th day of September, 1954.

L. L. Forbes Construction Company

s/ A. W. Bodine (Seal)

Principal

A. W. Bodine, Partner

In the Presence of:

The Home Indemnity Company

Surety (Seal)

By s/ Frank Distal

Attorney-in-Fact

State of)
) ss.

County of)

On this.....day of....., 19.....
Individual—
Principal before me personally appeared the within named
.....to me known, and known
to me to be..... the individual
described in and who executed the within bond, and
.....acknowledged to me that.....he.....
executed the same.

Notary Public
County.

State of Arizona)
) ss.
 County of Maricopa)

On this 30th day of September, 1954, before me ^{Firm—} personally appeared A. W. Bodine a member of the ^{Principal} firm of L. L. Forbes Construction Company to me known and known to me to be the individual described in and who executed the foregoing instrument, and he duly acknowledged to me that he executed the same as and for the act and deed of the said firm.

s/ Lola E. Davis

Notary Public
 County.

My Commission Expires Mar. 1, 1957

County of)

) ss.

State of)

On this.....day of....., 19.....

Corporation—
Principal

before me personally appeared.....

with whom I am personally acquainted, who, being by
me duly sworn, did depose and say:

That he resides at.....that he is the.....

of the..... the corporation

described in and which executed the foregoing instru-
ment; that he knows the corporate seal of said cor-
poration; that the seal thereto affixed is such cor-
porate seal. that it was so affixed by order of the
Board of Directors, and that he signed his name
thereto by like order......
Notary Public
County.

No. 15,651

In the

United States Court of Appeals

For the Ninth Circuit

AMERICAN RADIATOR AND STANDARD SANITARY CORPORATION, a corporation,

Appellant,

vs.

L. L. FORBES and A. W. BODINE, Doing Business as L. L. FORBES CONSTRUCTION COMPANY, and THE HOME INDEMNITY COMPANY, a corporation,

Appellees.

Joint Brief for the Appellees

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PAUL P. O'BRIEN, CLERK

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COMPANY, and THE HOME INDEMNITY
COMPANY, a corporation,

Appellees.

Joint Brief for the Appellees

STATEMENT OF THE CASE

Appellant's Statement of the Case should, we believe, be supplemented and clarified as follows:

1. As clearly appears from the amended complaint (R.3), the action is upon the contractor's bond executed by the defendants Forbes and Bodine, as principals, and the defendant, The Home Indemnity Company, as surety. The amended complaint alleges that the bond was conditioned upon the faithful performance of the contract and the satisfaction of all bills, charges and liens for labor and materials incurred in the performance of the contract. However,

the bond, a copy of which is attached to Appellant's Brief (Appendix, Page XIII), was conditioned upon the indemnification of the School District against loss or damage caused by the failure of the principal to faithfully perform the contract; and said bond expressly provided that no right of action should accrue upon or by reason of the bond to or for the use of anyone other than the obligee therein named.

2. The statement at the beginning of Appellant's Statement of the Case that the action was brought by American Radiator to recover the unpaid balance of the purchase price of materials which it furnished for installation for the construction of the classroom additions might be taken to imply that materials were furnished by Appellant with the intent or purpose on its part that they were to be installed and used in the construction of the additions. This does not anywhere appear in the record. The record, as appears in the Agreed Statement of Facts (R.14), is that Bachman, a subcontractor, purchased plumbing materials and supplies from the Appellant and that some of the materials were incorporated in the classroom addition, and it nowhere appears that there was any intent, purpose, knowledge, or understanding on the part of Appellant that any of the materials were to be so installed or used.

3. The statement of Appellant on Pages 6 and 7 of its Brief of the facts on which the question of liability should be based should be modified. Numbers 1 and 2 at the bottom of Page 6 should be worded as follows: 1. There has been a written contract between the general contractor and the School District, in the form involved herein (Appendix to Appellant's Brief, Page I), which, among other things, provided that, except as otherwise noted in the contract, the contractor should provide and pay for all materials,

labor, tools, water, power and other items necessary to complete the work, and which contract further provided that certain items, such as surveys, certain permits, licenses and easements and certain insurance should be secured and paid for by the owner. 2. The general contractor has accepted payment of the statutory redemption fund without having furnished to the public authority any receipt or lien waiver from the party who sold materials to a subcontractor, evidencing payment for the materials, but the general contractor, before accepting payment of said statutory redemption fund, paid the subcontractor for the materials and furnished to the public authority a satisfactory receipt of the subcontractor evidencing such payment by the general contractor to the subcontractor.

Further, there should be added to the Statement of Appellant of the facts involved in said question of liability, following Paragraph 3 at the top of Page 7 of its Brief, additional Paragraphs 4 and 5 as follows: 4. The action brought by the seller of materials to the subcontractor is an action on the bond of the general contractor, which bond was conditioned for the indemnification of the obligee, the school district, against loss or damage caused by the failure of the principal to satisfactorily perform the contract, and which bond expressly provided that no right of action should accrue upon or by reason of the bond to or for the use of anyone other than the obligee therein named. 5. The statute makes no provision for a bond to be furnished conditioned for the payment of labor or materials.

SUMMARY OF ARGUMENT

Forbes' contract with the School District was a contract between the School District and the general contractor and was not a contract for the benefit of materialmen supplying

materials to a subcontractor and the contract conferred no third party beneficiary rights upon such materialmen. To come within the orbit of the third party beneficiary rules, it must appear that the contracting parties intended to benefit the third party by said contract. No such intent is present here.

Appellant, American Radiator, in this case sold materials to the subcontractor, Bachman, in reliance solely on the credit of said subcontractor and not in reliance upon any provisions contained in the contract or in the bond executed by Forbes to the School District.

II.

There is no Arizona statute directing a School District to require a bond conditioned for the benefit of material suppliers of subcontractors, such as Appellant here. The Arizona statute merely calls for a bond "conditioned upon the faithful performance of the contract". The bond executed in the instant case complies with this statute. In addition the bond clearly states that it is an indemnity bond, the sole purpose of which is to indemnify the Board of Supervisors or the School District against loss or damage directly caused by the failure of the Principal (Forbes) to faithfully perform said contract. Further, the bond expressly provides: "that no right of action shall accrue * * * for the use of anyone other than the Obligee herein named". It is obvious that a bond, which is of the type furnished in this case and which contains the above provisions, does not inure to the benefit of a third party, and Appellant, being a third party, is not entitled to sue and recover on the bond.

III.

The Arizona statute, governing contracts for the erection of public buildings, requires the Board of Supervisors to

retain ten (10) percent of all estimates as guarantee of the complete performance of the contract, to be paid to the contractor within sixty-five (65) days after completion, or on filing of notice of completion of the contract, provided the contractor has duly furnished the agent satisfactory receipts for all labor and material bills and waivers of liens from any and all persons holding claims against the work.

The statute definitely states that the 10% of the contract price is to be paid to the contractor within 65 days after completion and does not state "not prior to 65 days from completion of the contract" as set forth in appellant's brief. Pursuant to a contract between Forbes and the subcontractor, W. M. Bachman, dba Bachman Plumbing Company, and for an agreed sum, Bachman undertook to furnish all necessary labor and material required for the installation of certain plumbing equipment in the erection of the public school. Forbes paid the subcontractor Bachman in full for the labor and materials furnished by the subcontractor Bachman, and thereafter Forbes furnished a satisfactory receipt from the subcontractor Bachman to the Board of Supervisors. Forbes therefore fully complied with the contract and there was no breach thereof on which any action could be maintained. Forbes further fully complied with the statute and did not receive the retention fund in violation of the statute; thus, no constructive trust could be impressed on the retention funds in favor of the appellant.

ARGUMENT

- I. The Contract Between Forbes and the School District Was for the Purpose of Delineating the Obligations to Be Undertaken by Each of the Parties to Said Contract—and Was Not Intended to Confer a Benefit Upon Third Parties.**

The first argument relied upon by appellant is to the effect that the contract between the School District and

the general contractor conferred third party beneficiary rights upon appellant. To support this contention, appellant quotes an excerpt from Article 1 of the contract and Article 3 of the General Conditions.

Appellees contend that these Articles were obviously inserted to delineate the relative obligations of the parties to the contract and to negate any idea that the School District would furnish materials for the job. Just the same as Article 5 of the General Conditions on the other hand provides that the owner (School District) should furnish all surveys unless otherwise specified, and again that the owner was to secure and pay for all permits, licenses, etc. It is manifest that by these clauses the parties intended to set out their mutual duties and obligations towards *each other*. Article 3 of the General Conditions also sets out that the contractor was to pay for all power necessary to complete the work. Was this clause inserted for the benefit of the Arizona Public Service Company? Did the parties intend to create a direct and primary obligation in favor of Arizona Public Service by having provided that the contractor was to pay for the power necessary to complete the work? This clause was inserted merely to clarify the fact that the School District was not to furnish the power necessary in the erection of the building, and that the contractor would have to supply the power.

The heading of Article I of the contract is entitled: "Scope of the Work". This, in conjunction with the whole of said Article is strong evidence of the fact that the primary purpose of the agreement and attendant documents, was to define and limit the duties and obligations of the two *contracting parties*.

The intent of the parties is further evidenced by the fact that the bond in the instant case was executed simul-

taneously with the contract and the provisions of said bond, accepted by the School District, provided that no right of action shall accrue to or for the use of anyone other than the obligee. If it was the intent of the School District and the contractor that third parties should be benefited under the contract, then most certainly a protective clause would have been inserted in the bond for the benefit of such third persons.

A reading of the contract as a whole and the attendant documents and an examination of the circumstances surrounding its execution make it clear that the contracting parties had no intention whatever to confer benefits upon any person, such as the appellant, who is a stranger to the contract.

As to the contract itself, the rule is well established that parties are presumed to contract for their own benefit, and that one not a party to a contract will not be permitted to claim thereunder unless it clearly appears that the parties to the contract intended it to be for his benefit. *Citizens National Bank v. Texas and Pacific Railway Co.*, 136 Tex. 333, 150 S.W. 2d 1003; *Knox v. Ball*, 144 Tex. 402, 191 S.W. 2d 17; *Electric Appliance Co., v. United States Fidelity and Guaranty*, 110 Wis. 434, 85 N.W. 648; 12 Am. Jur., page 834; 17 C.J.S. pages 1143 and 1220.

In the instant case Forbes, the principal contractor, is not liable for materials furnished to a subcontractor because no privity of contract exists between him and materialmen. 17 C.J.S., page 1143; *Board of Public Education and Wilmington, etc., v. Aetna Casualty & Surety Company*, 34 Del. 355, 152 Atl. 600, 603; *Kruse v. Wilson*, 3 Calif. App. Rep. 91, 84 Pac. 442; *McKenzie v. Neale Construction Co.*, 75 Wyo. 175, 294 Pac. 2d 355; *Llewellyn Iron Works v. Reed, et al*, 123 Calif. App. Rep. 607, 11 Pac. 2d 657; *Russell Lumber &*

Supply Co. v. Grooms, 231 Ky. 544, 21 S.W. 2d 835, 13 C.J. page 713, Note 57; 17 C.J.S., page 1143.

Some of the requirements in order to construe a contract as creating a third party beneficiary obligation are set out in 17 C.J.S., page 1127, as follows:

“That the parties must have clearly intended the contract to be for the benefit of the third person * * * is one of the most commonly expressed limitations on the rule, * * *”

and on page 1129,

“The intent to benefit the third person must clearly appear from the language of the agreement, * * *”

and on page 1131,

“It has been held that the contract must have been made completely and primarily for the benefit of the third person * * *.”

American Jurisprudence, Volume 12, Contracts, page 833, states the rule as follows:

“A third person for whose direct benefit a contract was entered into may sue for breach thereof; but if the benefit is only incidental, he may not. It has been asserted that before a stranger can avail himself of the exceptional privilege of suing for a breach of agreement to which he is not a party, he must at least show that it was intended for his direct benefit. It must appear, in order that a third person may derive a benefit from a contract between two other parties, that the contract was made and entered into *directly and primarily for the benefit of such third person*. * * *” (Emphasis supplied.)

In the instant case, none of these requirements is present. It is obvious that the School District was only concerned with getting its building constructed. The clause saying

that the contractor shall provide and pay for all materials, labor, tools, water, power and other items necessary to complete the work was inserted to make clear that the materials, labor, tools, water, power and other items necessary in the erection of the building were to be furnished by the contractor and not by the School District, just the same as the provisions that the School District would furnish and pay for surveys, permits, licenses, etc., indicate the items which the School District was to pay. Nowhere is there any mention of any third party, and nowhere, either expressly or by implication, is there any intention shown to confer a benefit on some third party. Rather, every circumstance points to the contrary and indicates that the parties were concerned only with themselves.

It is interesting to note that appellant has advanced no argument whatsoever, nor has he cited any provisions of the contract, which support his contention that the contract involved herein was one for the benefit of appellant. In all probability it is because of this void that from the very inception of this action appellant has never asserted any rights under the contract. Appellant's amended complaint alleges a claim based solely on the bond and not on the contract. In support of his first contention appellant relies entirely on cases which are clearly distinguishable from the instant case as we will show and which are cases involving interpretation of provisions of bonds and not of contracts.

We unhesitatingly submit that there is nothing in any of the cases cited by appellant in support of his first argument that by any form of analogy could it be logically concluded that the courts of Arizona would hold for the appellant in the instant case.

The decision of the Court in the case of *Webb v. Crane*, 52 Ariz. 299, 80 P.2d 698, cited by appellant was clearly

based upon the provision contained in the bond involved in that case. The bond contained a provision for the payment of laborers and materialmen, the bond was conditioned for their benefit, but did not in terms give them a direct right of action on the bond. Since the bond contained a provision for their benefit, the Arizona Court simply allowed them to have a right of action in order to enforce and give meaning to the provision which had been inserted for their benefit. These facts are entirely different from the facts of the instant case. The bond with which we are concerned not only contains no provision for the benefit of laborers and materialmen, but recites that it is an *indemnity* bond only, and specifically provides that *no one* other than the named Obligee shall have any right of action thereunder.

A part of the opinion from *Webb v. Crane* which appellant quotes is as follows:

“The right of laborers and materialmen to recover on a bond executed in connection with public works or improvements, *where the bond contains a condition for their benefit and is intended for their protection*, although the public body is the only obligee named therein, and there is no express provision that such third parties shall have any rights thereunder, is affirmed by the great weight of authority.” (Emphasis supplied.)

The foregoing statement was taken by the Court from an annotation on this subject in 77 A.L.R. On page 106 of this very same annotation, that authority has this to say about the type of fact situation presented in the case at bar:

“It may be stated as a general principle that a laborer or materialman cannot recover on a bond executed by a contractor to the public body, *conditioned only to indemnify or hold harmless* the obligee against loss or damage resulting from the defaults of the contractor.” (Emphasis supplied.)

In the resume and conclusion of this annotation, on page 213, the law is stated to be that:

“According to the prevailing rule, the right of laborers and materialmen to recover on a contractor’s bond depends upon the terms of the instrument. It depends upon whether the bond is actually for the benefit of such persons, or is for the protection of the nominal obligee and merely incidentally benefits the third parties * * *”

“Where the bond is conditioned merely to indemnify and hold harmless the owner or public body, it seems, both by authority and reason, that it does not inure to the benefit of laborers and materialmen so as to enable them to recover thereon.”

In the case of *Knight & Jillson Co. v. Castle*, 172 Ind. 97, 87 N.E. 976, 27 L.R.A. (NS) 573, cited by appellant, a contract and bond with the following provisions was involved. The contract provided:

“Parties of the Second Part agree to pay for all labor and materials used in said work when due and that all labor done and materials furnished shall be of the best quality of their several kinds and the Parties of the Second Part agree to deliver said building to said First Party freed from all liens or right thereto.”

The bond entered into in this case reads:

“Whereas said Principal has entered into a written contract dated April 24, 1903, with said Obligee for the plumbing, steam heating and electric wiring for St. Joseph’s Catholic Church, a copy of which contract is hereto annexed. Now, THEREFORE the conditions of this obligation is such, that if the said principal shall faithfully perform said contract on their part, according to the terms, covenants and conditions thereof (except as hereinafter provided), then this obligation shall be void, otherwise to remain in full force and effect.”

The facts in the *Knight & Jillson* case show that Knight & Jillson Co. was a materialman who supplied material *directly to the general contractor*, rather than to the subcontractor as in the case at bar.

Further, the plaintiff in that action included, as a part of his complaint, the contract and bond; in addition, the plaintiff alleged that at the time he sold and delivered the materials to the contractor, said plaintiff had knowledge of the execution of the bond and relied upon the same to secure payment for the materials delivered to the general contractor. This, of course, indicates that the materialman unquestionably relied upon the bond and contract, and the provisions thereof, rather than the credit of the one to whom he supplied the materials, as in the case at bar. In the instant case, the appellant furnished the material to the subcontractor and appellant's recourse by virtue of the contract and bond was strictly an afterthought.

In the *Knight & Jillson case*, the Court in its opinion, speaking of third party beneficiaries contracts says that the third party beneficiary rules "are to be applied with discrimination respecting each particular case". It is obvious from the foregoing that each case, wherein a third party beneficiary question is raised, must be decided upon its own set of facts and the doctrine of stare decisis is of little benefit.

In the *Knight & Jillson case*, the provisions of the bond involved therein were entirely different from those of the bond involved in the instant case. Furthermore, the bond in the instant case is an indemnity bond and specifically limits any right of action therein to the named Obligee. Had this provision been a part of the bond in the *Knight & Jillson case*, we have no doubt that the Court there would have held differently.

The case of *Standard Acc. Ins. Co. v. Simpson*, 4 Cir., 64 F.2d 583 and the Annotations in 70 A.L.R. 308 (supplemented in 111 A.L.R. 311) referred to by the appellant in his first argument, refer to situations wherein a bond was given pursuant to statute, to secure payment for labor and materials furnished in the construction of a public building or other public improvement, or the bond itself provided that the contractor would pay when, and as due, all lawful claims for labor furnished, or materials and supplies furnished. Whereas, in the instant case, the contractor's bond is conditioned only to indemnify the named Obligee against loss or damage directly arising by reason of the contractor's failure to faithfully perform the contract; and there are no statutes in Arizona requiring a bond conditioned for the payment of labor and material.

Likewise, the cases of *United States Use of Hill v. American Surety Company*, 200 U.S. 197, 50 L.Ed. 437, 26 S.Ct. 168 and *City of Portland v. New England Casualty Co.*, 78 Ore. 195, 152 Pac. 253, cited by appellant in his Argument I, both involve statutes enacted primarily for the benefit of laborers and materialmen, and the contracts and bond entered into, contained similar protective provisions. Neither case is akin to the instant case, but will be treated more fully later in this brief.

In the case of *Hipwell v. National Surety Company*, 130 Iowa 656, 105 N.W. 318, cited in appellant's brief at page 19, a *statute* was construed that provided that when a bond or other instrument given to a State or County or other municipal or school corporation, or to any officer or persons, is intended for the security of the public generally, or of particular individuals, action may be brought thereon in the name of any person intended to be thus secured, who has sustained an injury in consequence of a breach thereof, except when otherwise provided. And where, in that case,

in a contract for the construction of a public building, the contractor agreed to pay promptly for all labor and materials used in the building and the bond was conditioned on compliance with all terms and conditions of the contract, the Court merely held that the failure of the contractor to pay subcontractors furnishing labor and materials, was a breach of the bond and authorized the subcontractors to maintain an action thereon *under the Iowa statute*.

The reference to 77 ALR 141, contained on Page 20 of Appellant's Brief, is preceded by the following text material: "The purpose and practical effect of *statutes* requiring of contractors for public work a bond for the benefit of laborers and materialmen is to give to such persons protection or security in lieu of, or analogous, to the mechanic's lien accorded it in a case of a contract between private individuals." (Italics added.) It is apparent from observation of the quoted text material that the cases cited thereunder deal only with situations where there is an existing statute that requires contractors to execute a bond for the benefit of laborers and materialmen. There is no such statute in the State of Arizona, consequently, these cases can have no bearing on any decision reached in the instant case.

Appellant has cited no cases where a statute similar to the Arizona statute has been interpreted. All cases cited by appellant include an explicit provision in either the statute or the bond requiring protection of laborers and materialmen. None of the cases cited appertain to interpretations of contracts which would in any way support appellant's contention that the contract of Forbes with the School District was for the benefit of materialmen. We will cite cases involving the interpretation of provisions in bonds in support of our second argument herein. These cases will be found to be more in point than any of the cases cited by appellant in support of his first argument.

II. Where the Condition of the Bond Is That the Bonding Company Shall Indemnify the Named Oblige and There Is No Statute Providing Otherwise, No Right of Action Accrues Upon the Bond to Anyone Other Than the Said Named Oblige.

The Bonding Company is the surety on the bond of Forbes. The obligee is the Board of Supervisors of Maricopa County, Arizona, acting for Glendale Union High School District.

The condition of this particular bond is as follows:

“* * * if the Principal shall *indemnify* the obligee against loss or damage directly caused by the failure of the Principal to faithfully perform said contract, then this obligation shall be void; otherwise to remain in full force and effect.” (Emphasis supplied.)

It will be seen that this is clearly an indemnity bond, and not a direct obligation or payment bond. In other words, it does not create a direct obligation to third persons, but is conditioned only upon indemnification of the Board of Supervisors or the School District against any loss. The Board and the School District have been dismissed from this lawsuit; consequently, no obligation or liability will be imposed upon them which could require indemnity under the bond.

It is impossible to see how anything could be more clearly expressed, than that this bond is designed only for the protection of the obligee, and that others are to be given no rights under it.

Since the bond which was actually given contained no provision for the benefit of appellant, let us see whether there was any duty, by statute or otherwise, for the School District to require a bond conditioned for the benefit of appellant. The bond was furnished in compliance with Section 10-610, A.C.A. 1939 as amended. This statute merely requires a bond

conditioned upon the faithful performance of the contract, and to be approved by the Board.

Nowhere in our statute is there anything stated which requires the School District to demand a bond conditioned for the benefit of material suppliers of subcontractors. Therefore, terms of the bond are not broadened by statute. The statute requiring the bond does not specify the form of the bond and does not require a bond conditioned for the benefit of material suppliers of subcontractors. Compare the Arizona statute with the statute in force in Iowa, which is a typical statute requiring a third party bond. Section 573.2 of the Code of Iowa reads as follows:

“Contracts for the construction of a public improvement shall * * * be accompanied by a bond, with surety, conditioned for the faithful performance of the contract, and for the fulfillment of such other requirements as may be provided by law. * * *”

And immediately thereafter, in Section 573.6, their statute further provides:

“The following provisions shall be held to be a part of every bond given for the performance of a contract for the construction of a public improvement, whether such provisions be inserted in such bond or not, to-wit:

1. The principal and sureties on this bond hereby agree to pay to all persons, firms, or corporations having contracts directly with the principal or with subcontractors, all just claims due them for labor performed or materials furnished, in the performance of the contract on account of which this bond is given,
* * *

The Iowa statute expressly and specifically sets out that third persons are to be protected by a public contractor's bond. No mandate of this sort is to be found in the Arizona statute.

The general rule is that in the absence of a provision in the statute as to the form or conditions of a bond required, such matters are left to the discretion of the authorities authorized to require the bond. See 78 C.J.S., Schools and School District, Page 1270, where it is said:

“In the absence of a provision in the statute as to the amount, form, or conditions of a bond required of a contractor with school authorities, such matters are left to the discretion of the authorities authorized to require the bond.”

Because our statute does not define the form or conditions of the bond referred to, it becomes apparent that the School District was free to select the type of bond they desired. This they have done, and the bond which they selected was not a bond conditioned for the benefit of third persons. Consequently, the bond is not varied by the statute, and construed in the light of the statute which required it, is in nowise changed or altered, and does not inure to the benefit of appellant. In 78 C.J.S. at Page 1271, the following statement of law is found:

“A bond for the faithful performance and to save the board harmless from loss resulting from the contractor’s breach protects the board from any claim against it on account of labor or material; a bond for faithful performance, *but not for payment of claims of laborers and materialmen, does not inure to the benefit of laborers and materialmen.*” (Emphasis supplied.)

There is one specific provision which forecloses the right of the appellant to recover on the bond. The bond contains this express limitation:

“PROVIDED, however, and upon the Express Conditions, the performance of each of which shall be a condition precedent to any right of recovery hereon:

* * * * *

"FIFTH: That no right of action shall accrue upon or by reason hereof to or for the use of anyone other than the Obligee herein named; that the obligation of the Surety is, and shall be construed strictly as one of suretyship only; * * *"

In *118 A.L.R. at page 78*, the rule is stated as follows:

"Laborers and materialmen cannot recover on a public contractor's bond conditioned merely to indemnify the named obligee against loss or damage resulting from the contractor's default in the performance of the contract, where the bond contains an express provision that no right of action shall accrue thereon for the use or benefit of anyone other than such obligee."

And in *78 C.J.S. at page 1279*, the rule is stated to be:

"A bond conditioned for the payment of laborers and materialmen may be so worded and construed to protect only the school district or other local school organization, *particularly where the bond expressly stipulates that no right of action shall accrue for the use or benefit of anyone other than the school authorities as obligee.*" (Emphasis supplied.)

And in *78 C.J.S. at Page 1283*, it is stated that:

"The liability of a surety on a bond given by a school contractor conditioned for the payment of laborers and materialmen is limited by the terms of its contract."

And again, in *78 C.J.S. at Page 1293*:

"In the absence of statute, the right to sue for the benefit of laborers or materialmen is dependent entirely on the terms of the bond, *and in the absence of a provision promising to pay laborers and materialmen, no such action can be maintained*, although where such provision exists, such an action is proper." (Emphasis supplied.)

A case exactly in point is *Massachusetts Bonding & Ins. Co. v. United States R. Corp.*, 97 S.W. 2d 596, 265 Ky. 661. The identical bond provisions are involved, the statute is almost identical, and the general situation is the same. A recovery by the materialman on the bond was denied.

In this case a public contractor's bond conditioned only to indemnify the named obligee against loss or damage directly arising by reason of the contractor's failure faithfully to perform the contract was held not to inure to the benefit of laborers and materialmen, where the contract stipulated that the contractor should provide and pay for all materials and labor necessary for the work, and that he should furnish a bond covering the faithful performance of the contract and the payment of all obligations arising thereunder, in such form as the owner might prescribe, where the bond as given did not embody any provisions for the benefit of third parties, but expressly provides that no right of action should accrue thereon to or for the use or benefit of anyone other than the obligee named therein. This case in all of its salient features is identical to the case at bar, and is very persuasive against the claim of appellant. The Court said, at Page 587:

"The right of materialmen to recover payment of their bills of the surety in bonds of this class usually rests upon the conception that they are made in part for their use and benefit, and the right of action inures to those materialmen directly against the surety. But there can be no such implication or conception here, for, in addition to the above-quoted clause, which merely bound the surety to indemnify the owner against loss or damage, it was very clearly stipulated to the contrary. Among the terms of the bond and suretyship is the following: 'That no right of action shall accrue upon or by reason hereof, to or for the use or benefit of any one other than the obligee herein named; that the ob-

ligation of the surety is and shall be construed strictly as one of suretyship only.' ”

Another case similar to the one at bar is *United States v. Farley, et al.*, 91 Fed. 474. In that case a contractor entered into a contract with the United States to construct certain wing dams and, to secure proper performance thereof, executed a bond, with sureties, to “promptly make full payments to all persons supplying them with labor or materials in the prosecution of the work provided in said contract”; the contractor entered into an agreement with a subcontractor that said subcontractor would furnish certain materials; the subcontractor supplied the materials and was paid in full by the contractor; however the subcontractor failed to pay his employees and they brought an action against the contractor and his surety on the bond given the United States. In holding for the defendants, the Court said:

“* * * In this case, therefore, the plaintiffs are not entitled to judgment in their favor, unless they fairly come within the terms of the bond itself, * * *” “Full payment having been made by (the contractor) to (the subcontractor) for the stone by him delivered and used in the work, (the contractor) have met and performed the conditions of the bond sued on, and there is no ground shown which would justify the court in holding that (the contractor) are bound to pay the wages of all the workmen employed by (subcontractor). Such a construction of the contract would result in preventing a contractor with the government from contracting in his own behalf for the delivery of any material by a third party, unless he was willing to assume the payment of all claims against the subcontractor, * * *. Having paid to (subcontractor) the full amount coming to him, (contractor) have performed all the conditions imposed on them or their sureties by the terms of the bond sued on. * * *” (Enclosures in parentheses substituted in lieu of names of parties.)

The case at bar contains no such requirements in the bond as does the cited case but in the instant case, it clearly appears that appellee paid the subcontractor in full for materials furnished; to hold appellee liable for materials supplied the subcontractor by appellant would, in the words of the *Farley* case, "result in preventing a contractor * * * from contracting in his own behalf for the delivery of any material by a third party, unless he was willing to assume the payment of all claims against the subcontractor * * *". It is submitted that no such harsh result was intended by the law.

The Supreme Court of Arizona recognizes the fact that the obligations of the bond cannot be extended beyond the plain terms of the bond unless the statute specifically requires it. In *Ward v. Johnson*, 72 Ariz. 213, 232 P.2d 960, a plaintiff attempted to recover against the bond of a police officer. The Court pointed out that if the bond had been an official bond as defined by statute, its terms would extend to the plaintiff and permit his recovery. It pointed out, however, that in the absence of a specific statute giving the plaintiff the benefit of the bond, he was not covered. Said the Court at Page 215 of the Official Reporter:

"Although there are some jurisdictions not in accord, the prevailing and foregoing view is that the obligation of a surety on its bond cannot be extended outside the terms of the instrument itself. The rule is well stated in *United States Fidelity & Guaranty Co. v. Crittenden*, 62 Tex. Civ. App. 283, 131 S.W. 232; '* * * Unless there be some express provision of law, which would be read into the bond as a part thereof, authorizing suit upon such official bond by an individual for a wrong done him by an officer, then the well-settled principle of law that the obligation of a surety cannot be extended beyond the terms of his bond nor to one not a party thereto would seem to be applicable, as the bond only created

relations between the city as an entity which the official represented and such official * * *. See also Carr v. City of Knoxville, for use of Monday, 144 Tenn. 483, 234 S.W. 328, 19 A.L.R. 69; City of Eaton Rapids, to use of Snyder vs Stump, 127 Mich. 1, 86 N.W. 438; Alexander v. Ison, 108 Ga. 745, 33 S.E. 657; Cushing v. Lickert, 79 Neb. 384, 112 N.W. 616; District of Columbia, to use of Langellotti v. Federal & Deposit Co. of Maryland, 50 App. D.C. 309, 271 F. 383."

Counsel relies on *Webb v. Crane Co.*, 52 Ariz. 299, 80 P.2d 698. The difference is that in the *Webb* case there was a bond which expressly gave third parties a right to sue on the bond directly. In the *Indiana* case referred to by appellant in its brief, the right to sue third persons was extended by interpretation where the bond was silent on the subject. Here the bond is *not* silent, but it specifically provides that third persons cannot sue upon it. Likewise its condition shows that it is strictly an indemnity bond for the protection of the obligee and no one else.

In the case of *United States Use of Hill v. American Surety Co.*, 200 U.S. 197, 50 L.Ed. 437, 26 S.Ct. 168, cited by appellant, the contract provides that the prime contractor "shall be responsible for and pay all liabilities incurred in the prosecution of the work for labor and material." The bond in connection therewith provided that if the prime contractor "shall promptly make full payments to all persons supplying it labor or materials in the prosecution of the work provided for in said contract, then the above obligation shall be void and of no effect; otherwise to remain in full force and virtue." The facts in this case show that the principal contractor entered into a written contract with the United States for the construction of certain observation towers for an agreed compensation. The principal contractor then engaged a subcontractor to perform certain

portions of the work; this subcontractor in turn engaged another party to paint certain of the observation towers, and agreed to pay him, therefor, a certain sum. This latter party is the plaintiff in the cited case and was not paid for work performed; subsequently, he brought an action on the bond against the bonding company. In this instance there was a statute which specifically required that persons entering into formal contracts with the United States "shall be required before performing such work to execute the usual penal bond with good and sufficient surety with the additional obligation that such contractor or contractors shall promptly make payments to all persons supplying him or them labor and materials in the prosecution of the work provided for in such contract."

The Supreme Court in this case held that a materialman furnishing materials to a subcontractor was protected, but its reasoning was based solely on the provisions of the statute and the bond executed in accordance therewith; the Court in its opinion said:

"In view of the declared purpose of the statute, in the light of which this bond must be read, and considering that the act declares in terms the purpose to protect those who have furnished labor or material in the prosecution of the work, we think it would be giving too narrow a construction to its terms to limit its benefits to those only who supply such labor or materials directly to the contractor. The obligation is 'to make full payments to all persons supplying it with labor or materials in the prosecution of the work provided for in said contract.' This language read in the light of the statute, looks to the protection of those who supply the labor or materials provided for in the contract, and not to the particular contract or engagement under which the labor or materials were supplied."

The *City of Portland v. New England Casualty Company*, 78 Oregon 195, 152 P. 253, also cited in appellant's brief, is similar to the *Hill* case and was based primarily upon the wording of a somewhat like statute which required that bonds be executed for the protection of all laborers and materialmen. The statutes of Arizona merely require that the contractor furnish a bond in the amount of the contract conditioned upon the faithful performance of the contract. Arizona has no statute which directs or requires the bond to be conditioned for the benefit of laborers or materialmen. It is, therefore, pointed out that this is a matter for legislative action, rather than a matter for judicial legislation. It is basic that the Courts cannot make the laws but may only interpret existing laws. If the State of Arizona desires bonds given for the protection of laborers and materialmen on public buildings or improvements, then it should so legislate and phrase a statute accordingly, requiring, as in the *Hill* case, "that such contractor or contractors shall promptly make payments to all persons supplying him or them labor and materials in the prosecution of the work provided for in such contract".

From the foregoing authorities, it is clear that a bond which is of the type furnished in this case does not inure to the benefit of appellant. The only cases which have ever allowed a third party to recover on a bond of this type, have been in jurisdiction where there was a statute which expressly and unequivocally required all public bonds to be conditioned for the benefit of third parties. And even when this was the situation, the cases are evenly divided as to allowing recovery; some courts reading such a statute into the bond, and other courts refusing to do so because that would create a new and different contract for the parties.

In the instant case, since Arizona has no statute which directs or requires the bond to be conditioned for the benefit of appellant, the bond as given is in harmony with our statute, and there is no room whatever for doubt. The bond is not altered by our statute, and the terms of the bond give appellant no right of action.

It is submitted that under these circumstances the cases are clear that a third party, such as the appellant, may not recover on the bond.

III. Forbes Fully Complied With the Provisions of the Contract and the Statutes and Therefore There Has Been No Breach of the Contract and No Violation of the Statute and No Constructive Trust Could Be Impressed on the Retention Funds in Favor of the Appellant.

Section 10-610 of the 1939 Arizona Code, as amended, provides, in part: "Ten (10%) percent of all estimates as guarantee of *the complete performance* of the contract, to be paid to the contractor within sixty-five (65) days after completion, or on filing of notice of completion, or (of) the contract, provided the contractor has duly furnished the agent *satisfactory receipts* for all labor and material bills and waivers of liens from any and all persons holding claims against the work." (Emphasis supplied.)

On page 29 of appellant's brief, he states "that this 10% retention fund shall be paid to the contractor on the happening of both of the following events:

"(a) That 65 days have elapsed after completion of the contract."

"(b) That the contractor has duly furnished to the Board of Supervisors 'satisfactory receipts' for all labor and material bills and waivers of liens from any and all persons holding claims against the work."

As can be clearly seen from the language of the above quoted provisions of Section 10-610 of the 1939 Arizona Code, as amended, one of the conditions for the payment to the contractor of the 10% retention fund is not that 65 days have to elapse after completion of the contract, but merely that when, after completion, the contractor furnishes the Board of Supervisors with *satisfactory receipts* for all labor and material bills and waivers of liens from any and all persons holding claims against the work, the contractor shall be paid *within* the 65 day time limit. Therefore, if the contractor furnished to the Board of Supervisors *satisfactory receipts* for all labor and material bills, on the day after completion, the contractor would then be entitled to receive the 10% retention fund.

Forbes entered into a contract with a subcontractor, W. M. Bachman, dba Bachman Plumbing Company, for the said subcontractor to furnish all necessary labor and materials for the installation of certain plumbing equipment. The subcontractor purchased plumbing materials and supplies from the appellant, American Radiator and Standard Sanitary Corporation. The subcontractor, Bachman, was paid in full for all labor and materials by Forbes and, thereafter, Forbes furnished a satisfactory receipt from the subcontractor, Bachman, to the Board of Supervisors.

As the subcontractor Bachman was the only person that Forbes had contracted with to furnish all plumbing materials and labor, the subcontractor Bachman was then the only one entitled to receive payment for the plumbing materials and labor furnished, and the subcontractor's, Bachman's receipt for payment of all plumbing materials and labor furnished was a *satisfactory receipt* and was properly accepted by the Board of Supervisors. It is clear that Forbes has paid for all materials which were used in the

school building, and that Forbes had no dealings with the appellant whatever, and that Forbes in no way violated the provisions of the statute as to furnishing satisfactory receipts.

Bachman furnished the material, he performed the labor, and he was entitled to the pay. The one entitled to the compensation is the one with whom Forbes directly contracted and who, in turn, supplied the materials and the labor for the job. Unquestionably, a receipt from Bachman was a "satisfactory receipt".

The ten (10) percent retention fund clause in the statute was inserted for the protection of the public body, inasmuch as it provides that the ten (10) percent "shall be retained * * * as guarantee of the complete performance of the contract". This clause surely was not inserted as a guarantee for the payment of third persons.

Appellant contends that the latter part of the statute, Section 10-610 of the 1939 Arizona Code, as amended, which requires the School District to retain ten (10) percent of the estimates until satisfactory receipts have been furnished, has somehow been violated. This provision of the statute merely covers the procedure to be followed by the School District, in letting contracts and provides a means for the School District to protect itself by withholding moneys until the building is satisfactorily completed.

Appellant seems to be of the opinion that the purpose of Section 10-610 of the 1939 Code, as amended by the 1952 Supplement, was to protect such materialmen as appellant hereinasmuch as a lien could not be enforced against public buildings. This Section is contained in Article 6 of the 1952 Supplement, which Article is titled—"County, Municipal, and School District Indebtedness"; Section 10-610 bears the heading, "Erection of buildings for which bonds voted—

Method of payment." Construing the quoted titles in conjunction with the explicit wording of the section contents, it is very apparent that the sole purpose of the particular section was to provide for the manner in which payment was to be made on the contract and to provide adequate safeguards for the School District so that said District would be assured of proper completion of the work. If the Legislature had intended a result such as propounded by appellant, it would have been a very simple process to definitely word the statute accordingly.

The liability of a party to a contract is measured by the terms of the contract and there can be no liability arising as a result of a contract, unless there has been some breach of the terms of that contract by the party upon whom liability is to be imposed, 17 C. J. S. pages 942, 943 and 944. In the instant case there has been no breach.

One of the clauses which appellant contends has been violated requires the contractor to "provide and pay for all materials, etc.". The agreed facts are that the appellant sold the materials on credit to Bachman, and Bachman resold them to the general contractor who paid Bachman in full for them.

Bachman acquired title to the goods when he purchased them from the appellant, and then he resold them to the general contractor, who paid him in full. Thus, all materials which went into the work have been paid for by the general contractor, and he has in no way violated the clause of his contract requiring him to pay for all materials.

It is clear that appellant has no claim against anyone other than the subcontractor. This was the person with whom it dealt, the person to whom it sold the goods, and the person to whom it saw fit to advance credit. It is undisputed that Forbes has fully paid Bachman for these mate-

rials. His contract surely did not require him to pay twice for the same goods.

If appellant's contention were to be accepted, there would be no limit to how far back along the chain of credit one could go, and still come in and say that the goods which went into the school building were "not paid for". If appellant's claim is good, then the claim of a steel mill which sold steel on credit to the appellant, or the claim of an ore mine which sold ore on credit to the steel mill, would be equally good. This is not the law, and no citation of authority is necessary to sustain the point that the sale of property does not carry with it the obligation to discharge a personal debt, which the seller may have incurred to another when he purchased the property.

The last argument advanced by appellant is that there is a "constructive trust" as to the money which the School District paid to Forbes. A constructive trust is a trust "ex maleficio", or "ex delicto". It only comes into being when there has been a wrongful or illegal act. If there has been no wrong or illegal act, there can be no constructive trust.

In its brief, appellant points to the case of *Western Lumber and Pole Co. v. City of Golden*, 23 Colo. App. 461, 130 Pac. 1027, as authority for the imposition of a constructive trust. In that case, the Court, speaking of the statute, says as follows:

"The title of the act here under consideration reads as follows: 'An act to secure the payment of claims of laborers, subcontractors, and others performing labor and furnishing materials upon public works constructed under the authority of cities, incorporated towns and school districts.' It is manifest from the title of the bill that its purpose was to secure the payment of claims for which the city was not theretofore, under pre-existing laws, liable." (Emphasis supplied.)

The Court goes on and discusses the rights given by the statute, the new duty which is expressly imposed on the City by the statute, and the new obligations which this statute created. The distinctions between the Colorado statute and our Arizona statute are obvious.

The Colorado statute declares that its express purpose is to secure the payment of claims of laborers and those furnishing material for public works; and that statute specifically directs the public agency to retain certain amounts in order to satisfy the claims of the laborers and materialmen. This purpose is expressly declared, and the statute imposes a duty on the public agency to see that claims of laborers and materialmen are satisfied. It sets forth how they shall file claims, how they shall be paid, and so on. How different this is from the Arizona statute which appellant is attempting to distort to that purpose, and in which no such purpose is expressed and no such duty is imposed. Our statute is primarily designed for the protection of the public agency and is designed to assure the public agency of the satisfactory completion of the work by the contractor. There is nothing in our statute which required the school district to insert provisions in its contract for the benefit of appellant, or to otherwise act for the benefit of appellant in any way.

Consequently, that case has no bearing or application upon the instant case because our statute contains no such provisions.

In discussing the rights of a materialman in and to the statutory retained percentage, due to a contractor from a school district, C.J.S. in Volume 78, at Page 1316, says:

“In the absence of statute conferring the lien, the money due from the district or other local school organization to the contractor is not subject to a lien in favor of subcontractors, laborers, or materialmen, but

in a number of jurisdictions such lien is conferred by statute.”

The Colorado statute does set out a method whereby laborers and materialmen can assert a lien or claim to such fund. The Arizona statute does not.

No law was violated by the payment or acceptance of this fund. In this respect, we have heretofore shown that neither the statute, contract, or bond, conferred any rights upon appellant, or created any obligation on the part of the School District or the General Contractor towards appellant. Suffice it to note that constructive trusts are creatures of equity, and are not to be invoked except in aid of equity. Constructive trusts are a wrong-rectifying device, and unless there has been some wrong, there can be no constructive trust.

CONCLUSION

In conclusion, we would like to make the observation that one person ought not to be made to pay the debt of another, except upon a clear and satisfactory showing that he obligated himself to do so.

In this case, we have shown that neither by the contract, the bond, nor the statute, was any such obligation undertaken. We have shown that the law imposes no liability, and the inherent equity of the situation is likewise in accord with this position. If a loss has occurred to appellant, appellant alone is responsible for that loss. It was under no obligation to sell goods on credit to Bachman. If it wanted safeguards, it could have obtained them for the asking. Instead of this, appellant indiscriminately advanced credit and now is attempting to fasten a loss, caused by its own improvidence, upon innocent persons.

Justice demands that the appellant look for its payment to the person to whom it chose to advance credit, and not to another. The judgment of the District Court should be affirmed.

Dated at Phoenix, Arizona.

November 13, 1957.

Respectfully submitted,

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of Counsel.

No. 15,651

United States Court of Appeals
For the Ninth Circuit

AMERICAN RADIATOR AND STANDARD
SANITARY CORPORATION, a Corpora-
tion,

Appellant,

VS.

L. L. FORBES and A. W. BODINE, Doing
Business as L. L. FORBES CONSTRUC-
TION COMPANY, and THE HOME IN-
DEMNITY COMPANY, a Corporation,

Appellees.

Appeal from the United States District Court
for the District of Arizona.

APPELLANT'S REPLY BRIEF.

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FILED

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No. 15,651

United States Court of Appeals For the Ninth Circuit

AMERICAN RADIATOR AND STANDARD
SANITARY CORPORATION, a Corpora-
tion,

Appellant,

VS.

L. L. FORBES and A. W. BODINE, Doing
Business as L. L. FORBES CONSTRUC-
TION COMPANY, and THE HOME IN-
DEMNITY COMPANY, a Corporation,

Appellees.

Appeal from the United States District Court
for the District of Arizona.

APPELLANT'S REPLY BRIEF.

CONCERNING APPELLEES' STATEMENT OF THE CASE.

Both in the portion of the Appellees' Brief entitled "Statement of the Case" and throughout the argument, Appellees have stated that this action was brought solely upon the contractor's bond. This, of course, is wholly without foundation. We thought it was eminently clear from the pleadings, the record

and the organization of our opening brief that American Radiator seeks recovery against Forbes on the contract and against Forbes and the Bonding Company on the bond of which both the contract and the Arizona statute are integral parts. Surely there is nothing in the Amended Complaint which can be said to constitute an election to rely solely upon the bond. The Amended Complaint simply alleges that Forbes undertook to perform the construction of the school buildings pursuant to a contract with the School District and that the Bonding Company and Forbes executed and delivered to the School District a bond conditioned upon the faithful performance of the contract. The prayer is for judgment against the defendants and each of them in the sum claimed. Until the filing of Appellees' Brief, it was never suggested in their behalf that the issue of liability of Forbes under the contract was excluded from the consideration of the court. In fact, the Findings of Fact and Conclusions of Law which were prepared on behalf of Appellees contain two express Conclusions that the contract between Forbes and the School District was not for the benefit of third parties, including the plaintiff (R. 25). Surely there would have been no occasion to adopt Conclusions with respect to the legal effect of the contract if the action was only upon the bond.

Appellees have also from time to time questioned the propriety of our statement that the bond was conditioned upon the faithful performance of the contract by Forbes. It is true that the Bonding Company

attempted to limit its obligation to that of an indemnitor by adopting appropriate wording in the instrument. We do not, of course, assert that language of indemnification is not to be found in the bond. We do assert that *as a matter of law* the language of indemnification is figuratively obliterated by the express statutory requirement that a contractor's bond shall be conditioned upon the faithful performance of the contract. Having once articulated this reasoning, we thereafter adopted the short-cut device of stating that the bond furnished by the Bonding Company was conditioned on the faithful performance of the contract by Forbes.

Finally, Appellees take issue with our statement that the action was brought by American Radiator to recover the unpaid balance of the purchase price of materials which it furnished for installation in the classroom additions to Sunnyslope High School. Appellees assert that there is no justification in the record for such a statement and that it falsely implies that American Radiator furnished the materials with the intent that they should be installed and used in the construction of the school buildings. Appellees' assertion is without merit. The Agreed Statement of Facts contains the following statement:

"Bachman purchased plumbing materials and supplies from the plaintiff, American Radiator and Standard Corporation, *to install in the job.*"
(R. 15).

The court found this to be the fact in the exact words used in the Agreed Statement (R. 24). While

we do not regard the interpretation of this language as being controlling, we do assert that it fully justifies the inference that American Radiator furnished the materials in conscious anticipation that they would be installed in the job.

ARGUMENT.

I.

THE CONTRACT.

Because of Appellees insistence that this action is solely upon the bond, we assert again that American Radiator seeks recovery from Forbes because of his contractual undertaking to provide and pay for all materials necessary to complete the work. This liability would accrue whether there were a performance bond or not and forms the basis for a judgment against Forbes even if this court were to hold that the Bonding Company had successfully limited its liability by incorporation in the bond of what we regard as unlawful escape clauses.

The burden of Appellees' argument in respect to the legal consequences of the contractual undertaking to provide and pay for all materials necessary to complete the work is that the parties did not intend to benefit laborers and materialmen. This result is thought to arise from a reading of the provisions of the contract. We submit that there is no language in the contract which compels the conclusion that the parties intended to exclude recovery by materialmen.

The contractor has promised to provide and *pay for* all materials. Such an undertaking is fairly subject to the interpretation that the parties intended to extend the benefits of the contract to those persons entitled to be paid for the materials which the contractor agreed to furnish and for which he agreed to pay.

Appellees assert that we have advanced neither argument nor authority for our contention that the contract was intended for the benefit of third parties, including American Radiator. We are wondering whether Appellees' counsel have read that part of our brief which relates to an exhaustive analysis of the decision of the Supreme Court of Indiana in *Knight & Jillson Co. v. Castle*, 172 Ind. 97, 87 N.E. 976, 27 L.R.A. (N.S. 573 (Appellant's Brief, p. 15, *et seq.*). In that case, as we have stated, the contractor's agreement to pay for all labor and materials used in the work was held, as a matter of law, to be a third party beneficiary contract which inured to the benefit of a materialman even though the materialman, at the time of extending credit, had no knowledge of the existence of the contractual undertaking. In an effort to distinguish the *Knight & Jillson* case, Appellees say (Brief, p. 12) that American Radiator's attempted recourse against the contractor and the Bonding Company "was strictly an after-thought". Although we challenge the record for any evidence justifying that inference, under the rule of *Knight & Jillson*, the rights of the materialman are not affected by the circumstance that he did not know of or anticipate asserting rights which he had as a third party beneficiary of the underlying contract.

Appellees next seek to distinguish the *Knight & Jillson* case by saying that the bond was conditioned upon the faithful performance of the contract by the contractor. Two answers readily present themselves. The first is that Forbes is liable under the contract irrespective of the provisions of the bond. The second answer is that if the Bonding Company and Forbes had written a bond containing language which complied with the Arizona statute, it would have been conditioned upon the faithful performance of the contract by Forbes and would have been identical to the bond provided by the contractor in the *Knight & Jillson* case. Finally, Appellees attempt to avoid the *Knight & Jillson* case by pointing out that American Radiator supplied to a subcontractor, whereas Knight & Jillson Company supplied the general contractor. We anticipated this distinction in our discussion commencing at Page 17 of our opening brief in which we cited and quoted from the Fourth Circuit decision in *Standard Acc. Ins. Co. v. Simpson*, 64 F. 2d 583. Appellees dismiss the *Standard Accident* case with the comment that the bond was given pursuant to statute (Brief, p. 13). They misconceive the purpose of our citing the decision. We offered it for the purpose of assisting the court in construing Forbes' promise to provide and pay for all material necessary to complete the work. The issue, of course, is whether this language constitutes a promise to pay persons who supply materials to a subcontractor as distinguished from the general contractor. The *Standard Accident* case held that the agreement to "pay when and as due all lawful claims for labor performed or materials and

supplies furnished for use in and about the construction of said highway or highway structures” constituted a promise to pay persons supplying materials to a subcontractor. It happens that in that case the quoted language appeared in the bond rather than in the contract. While this fact might make a difference to the Bonding Company, it is all the same as respects the liability of the contractor whether he makes such a promise in his construction contract or in his bond.

Hipwell v. National Surety Co. 130 Iowa 656, 105 N.W. 318, 319, (Appellant’s Brief, p. 19), again provides a judicial construction of a written promise to “pay for all labor and materials used in and about the building”. Wholly apart from any statutory requirement with respect to bonds, the Iowa Supreme Court held that this language constituted a promise to pay persons who supplied materials to subcontractors. Unlike the *Standard Accident* case, the *Hipwell* case was concerned with the interpretation of the contract and not the bond.

II

THE BOND.

Here again, for the sake of clarity and because of apparent confusion on the part of the Appellees, we restate our position. We seek to hold both Forbes and the Bonding Company upon the principle that the contract contained Forbes’ promise to pay the claims of persons supplying materials to a subcontractor, that if Forbes and the Bonding Company had written

a bond conditioned on the faithful performance of the contract by Forbes (as they were compelled to do under the provisions of the Arizona statute) the obligation of the parties under the bond would have been to pay material suppliers to subcontractors and that, as a matter of law, the statutory requirement for a performance bond made the bond a performance bond in spite of any conflicting language contained in the instrument.

The only way in which Forbes and the Bonding Company can possibly hope to avoid liability under the bond is by successfully asserting that the escape clauses are valid. We are entirely in agreement that if the bond is to be enforced only in accordance with its express language, the Bonding Company is not liable. What we do not understand is how Appellees can hope to avail themselves of the escape provisions of the bond when admittedly their insertion in the instrument was wholly repugnant to the express requirement of the statute pursuant to which the bond was furnished. In our view, as we had hoped to demonstrate by our opening brief, if a contractor and a surety company execute and deliver what purports to be a performance bond and in compliance with an express statutory command, any efforts which they may make between themselves by a written instrument to change it into an indemnity bond or to limit the obligation of the surety to something less than the undertakings of the contract ought to be looked upon as unlawful and void. The only case which Appellees have cited in pretended support of this position is *Massachusetts Bonding & Ins. Co. v. United States R.*

Corp., 265 Ky. 661, 97 S.W. 2d 586. In that case the contract required the contractor to furnish a bond covering the faithful performance of the contract. The bond which was in fact furnished contained limitations which were not contemplated by the terms of the contract. As in the case at bar, the parties limited the condition of the bond to the indemnification of the School District against loss or damage arising out of the failure of the contractor to perform. The court readily conceded that if the parties had furnished a performance bond as required by the contract, the materialmen could have recovered. It held, however, that if the parties furnished a bond which did not meet the requirements of the contract, the surety could limit its obligations to the express condition of the instrument. The significant difference is, of course, that in the *Massachusetts Bonding* case the duty to furnish a performance bond arose only out of the contract and not out of statute as did Forbes' duty. We are not persuaded that Kentucky would follow the rule of the *Massachusetts Bonding* case if the duty to furnish a performance bond were created by law rather than by agreement. In cases in which the parties furnish a true performance bond in compliance with the contract, Kentucky holds both the contractor and the surety liable to materialmen. See, for example, *Royal Indemnity Co. v. International Time Recording Co. of New York*, 255 Ky. 823, 75 S.W. 2d 527, in which the contract provided that the contractor "will promptly pay for all labor performed and all material used or furnished in completing said work and carrying out this contract."

Appellees rely heavily upon a series of quotations from 78 Corpus Juris Secundum which in general relieve a surety of liability on a contractor's bond which is conditioned merely on the indemnification of the named obligee. None of these quotations purports to hold that a surety can so limit its liability in the face of an express statutory requirement for a general performance bond. For example, the quotation from 78 C.J.S. at p. 1293 opens with the words "In the absence of statute . . ." At Page 17 of Appellees' Brief is a quotation of the headnote appearing in 78 C.J.S. at p. 1271. This headnote states in part, ". . . a bond for faithful performance, but not for payments of claims of laborers and materialmen, does not inure to the benefit of laborers and materialmen". This, of course, begs the question for the reason that a faithful performance bond is in law one for the payment of claims of laborers and materialmen if such a promise is found in the contract whose performance the bond guarantees. This is more precisely spelled out in the text following the quoted headnote in which the author says (p. 1272):

"Moreover, a bond securing faithful performance of a contract, providing that the contractor should provide all materials and perform all labor *but not providing that he will pay for such materials and labor*, does not inure to the benefit of materialmen and laborers." (Emphasis supplied.)

In our case, of course, Forbes agreed both to provide and to pay for materials and labor. The text would appear to be conclusive authority for recovery by American Radiator.

Appellees also rely on the early decision of the Circuit Court for the Northern District of Iowa in *United States v. Farley*, 91 Fed. 474, in which an undertaking in the bond to pay all persons supplying the contractor with labor or materials was held to extend to direct suppliers to the contractor but not laborers employed by a subcontractor. Reference to Shepard's Citator would have led Appellees to the decision of the Court of Appeals for the District of Columbia in *United States v. James Baird Co.*, 73 F. 2d 652, 654, in which the court said that the rule of the *Farley* case was discarded by the United States Supreme Court in 1906. For the last 51 years, bonds like the one considered in the *Farley* case are uniformly construed to protect persons who supply labor and materials to subcontractors even though they expressly cover only labor and materials furnished to the prime contractor.

At Page 22 of their brief, Appellees seek to distinguish *Webb v. Crane Co.*, 52 Ariz. 299, 80 P. 2d 698, on the purported ground that the Webb bond expressly gave third parties a right to sue on the bond directly. This is simply not the fact. At p. 304 of the Arizona Reports, the Supreme Court said:

“Neither the contract nor the performance bond itself gives in express terms a direct right of action on the bond to materialmen . . .”

Notwithstanding this circumstance, the court held that the bond was a third party beneficiary bond upon which the subcontractor's materialman could sue and recover.

The Arizona Supreme Court decision in *Ward v. Johnson*, 72 Ariz. 213, 232 P. 2d 960, cited at page 21 of Appellees' Brief, has no application to the issue now before the court. In that case, Johnson sued two Tolleson police officers and their bonding company for false arrest and imprisonment. Under the express provisions of the bonds, they ran solely to the town of Tolleson and did not inure to other persons who might be aggrieved by the wrongful act of the bonded officers. The bonds were not furnished pursuant to any statutory requirement. The court held that the surety, in the absence of a statutory provision to the contrary, could lawfully limit its undertaking on the bonds. By way of dicta, the court said that if the officers' bonds had been "official bonds", such obligations as are stipulated by the applicable Arizona statute relating to official bonds would have been imposed on the surety whether they had been inserted in the written instruments or not. Following the language quoted by Appellees, the Supreme Court said:

"The above rule is subject to the principle that all contracts are governed by the laws of the jurisdiction which exist at the time of their execution."

Actually, the most salient difference between the *Ward* case and the case at bar is that the police officers bonds were not, as here, given to assure the faithful performance of a contract containing express promises for the benefit of third parties.

III

THE CONSTRUCTIVE TRUST.

No purpose would be served by repeating our position in respect to this separate theory of recovery against Forbes. The essential difference between the parties seems to lie in the interpretation of the words "satisfactory receipts", as contained in the Arizona statute. Appellees insist that the requirement of the statute is met by obtaining from the subcontractor a receipt evidencing payment to him of the contract price. Obviously, the contract price includes insurance premiums, cost of complying with the Workmen's Compensation laws, overhead and profit to the subcontractor, as well as his material and labor costs. We cannot conceive how a receipt from the subcontractor could constitute evidence of payment of labor and material bills.

Again, the requirement of the retention of 10% of all estimates as a guarantee of the complete performance of the contract was intended, like the requirement for a performance bond, to provide separate assurance that the contractor would do everything which he promised to do in his written contract. If, as a matter of law, he is held to have promised to pay materialmen and laborers, then the retention requirement guaranteed the fulfillment of that promise.

Appellees' alarm over the possibility that a steel mill which provided raw materials for pipe or even a mining company which provided ore for the steel mill might seek the protection of the bond and of the statute is a departure from reality. Clearly, the pur-

pose of the Legislature in providing the guarantees of a performance bond and a retention fund was to safeguard materialmen and laborers who were deprived of a lien because of the public nature of the work. *Webb v. Crane Co.*, 52 Ariz. 299, 80 P. 2d 698. Unquestionably, a materialman like American Radiator supplying pipe and plumbing fixtures which are incorporated in a privately owned structure has the right to perfect and foreclose a lien. This is true whether the material is supplied to the general contractor or to a subcontractor. This right of lien has never been extended to a steel mill providing raw materials or to a mining company providing ore to the steel mill.

CONCLUSION.

Appellees are concerned with the supposed inequity of our position which seeks to compel Forbes to satisfy American Radiator when Forbes has already paid Bachman in full. Appellees forget that Forbes was in the best position to protect itself by one or both of two simple expedients. Forbes, like countless other general contractors, could have exacted from Bachman a bond conditioned upon the payment of labor and material bills, or he could have retained all or a part of the balance due Bachman until Bachman had furnished Forbes with receipts from his laborers and materialmen. The inequity of double payment is always decried by persons against whom mechanics' and materialmen's liens are asserted, but to date this defense has never been successfully asserted to defeat the fore-

closure of such liens. If Forbes paid Bachman in full without satisfactory evidence of the payment of American Radiator's bill, he paid at his peril. And it is of more than passing interest to note that in this case Forbes had actual notice by letter mailed two days after the completion of the job that American Radiator had not been paid.

For the reasons hereinabove stated, the judgment of the District Court should be reversed.

Dated, Phoenix, Arizona,

November 29, 1957.

Respectfully submitted,

PHILIP E. VON AMMON,

Attorney for Appellant.

FENNEMORE, CRAIG, ALLEN & McCLENNEN,

Of Counsel.



No. 15652

United States
Court of Appeals
for the Ninth Circuit

*See also
Vols. 2931 and
3033
(No. 14705)*

UNITED MERCURY MINES COMPANY,
a corporation, Appellant,

vs.

BRADLEY MINING COMPANY, a corporation,
Appellee.

Transcript of Record

Appeal from the United States District Court for the
District of Idaho, Southern Division

FILED
SEP 25 1957



No. 15652

United States
Court of Appeals
for the Ninth Circuit

UNITED MERCURY MINES COMPANY,
a corporation, Appellant,
vs.

BRADLEY MINING COMPANY, a corporation,
Appellee.

Transcript of Record

Appeal from the United States District Court for the
District of Idaho, Southern Division

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THEORY OF THE EARTH AND ITS HISTORY

CHAPTER I

THE EARTH AND ITS HISTORY

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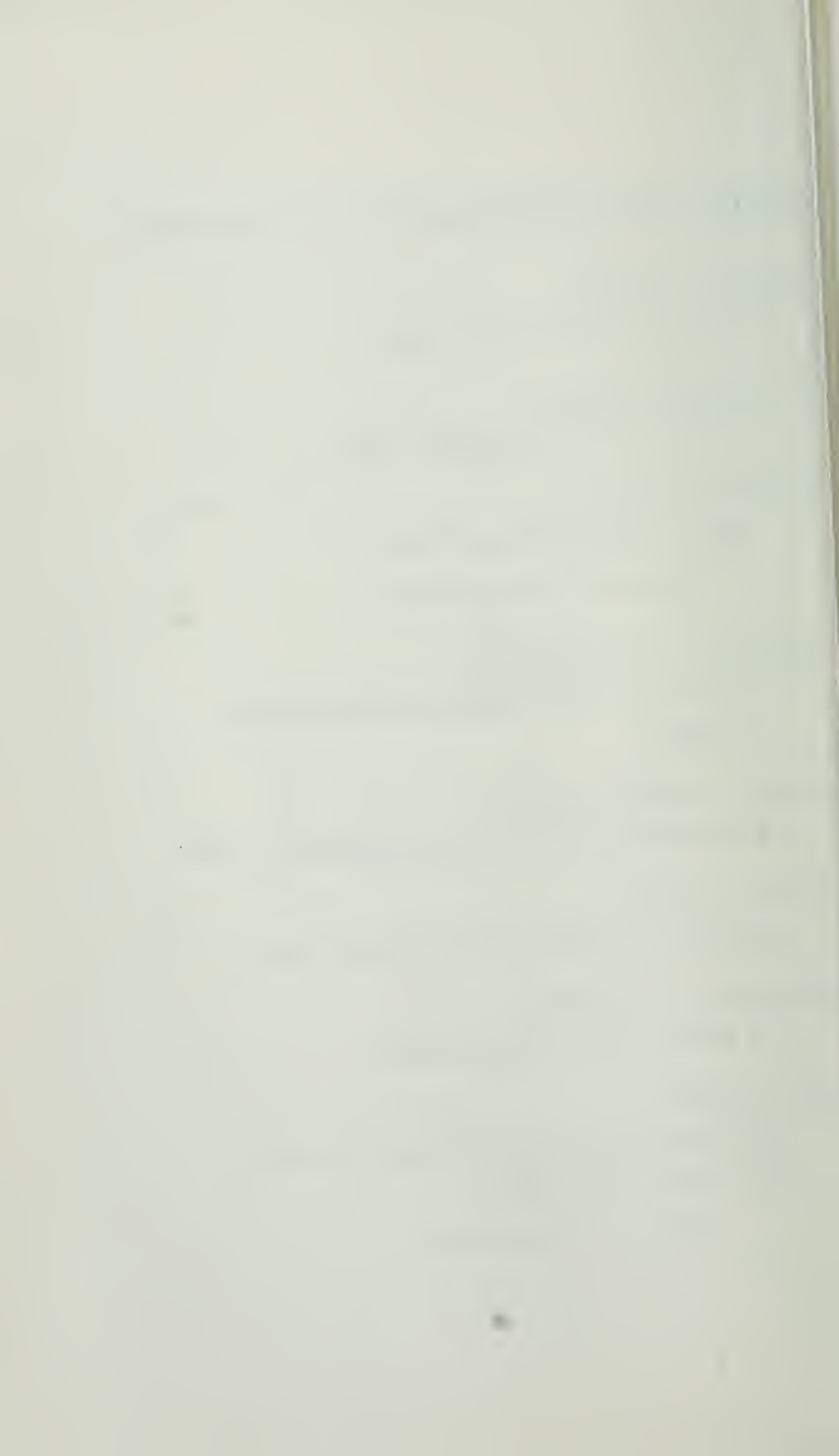
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In the District Court of the United States for the
District of Idaho, Southern Division

No. 2854

UNITED MERCURY MINES COMPANY, a cor-
poration, Plaintiff,

vs.

BRADLEY MINING CO., a corporation,
Defendant.

COMPLAINT

Comes now the plaintiff and complains of the de-
fendant and alleges:

I.

That at all times mentioned herein the plaintiff was and now is a corporation organized and existing under and by virtue of the laws of the State of Idaho and is a citizen and resident of said State; that at all times herein mentioned the defendant was and now is a corporation organized and existing under and by virtue of the laws of the State of California and is a citizen and resident of said State, but qualified to do business and doing business in the State of Idaho in full conformity with the laws of said latter State relating to foreign corporations doing business therein.

II.

That on or about the 31st day of December, 1941, the plaintiff as first party and the defendant as sec-

ond party entered into, made and executed a written conveyance, Royalty Agreement and Option, a copy of which is hereunto annexed, marked Exhibit 1, and by this reference made a part hereof. That among other things by said instrument the plaintiff, in consideration of certain royalties to be paid by defendant, conveyed to defendant numerous mining claims and other property therein described, and the defendant covenanted, promised and agreed to and with the plaintiff:

“To pay to United (the plaintiff, herein) its successors and assigns, a royalty of five percent (5%) on all net smelter returns, net revenue, and net mint returns, as defined herein, upon and for all minerals, ores, metals or values, of any and every kind and character, mined, extracted or taken from the above described mining claims, or any part thereof, or from any lands, grounds or claims, lodes or deposits, within the exterior boundaries of said groups of claims; the payment of said five per cent (5%) royalty to begin with the first returns received on concentrates shipped from Cascade, Idaho, after midnight, December 31, 1941, and to continue thereafter for nine hundred and ninety-nine (999) years and as long thereafter as minerals, ores and values shall be extracted, mined or taken from the above described property, at the times and in the manner hereinafter provided; said royalty to be paid to United by depositing the same with the First Security Bank of Idaho, at Boise, Idaho, or at such other place as may be designated in writing by United, to the credit and order of United on or be-

fore the 20th day of the calendar month next succeeding the receipt by Bradley of said net returns as defined herein, the same to be so paid each and every month when any net smelter, mint, or other returns are received by Bradley, copies of all sales returns to be furnished United by Bradley."

That said instrument further provides that:

"By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

"By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals and values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho.

"By net mint returns, as used herein, is meant the amount paid by any United States Mint, branch or agency thereof, less all shipping and marketing costs from Cascade, Idaho.

"It is agreed that in addition to the deductions of railroad freight from Cascade, Idaho, to the smelter, market, or mint, that Bradley shall also be allowed to deduct from the net smelter, market, or mint returns Two Dollars and Fifty Cents (\$2.50) per ton for each ton of concentrates, ores, metals, or values hauled or shipped from the above described property to Cascade, Idaho, the said sum to be deducted from the net smelter, market or mint

returns before net royalty herein provided for is computed.

“It is also agreed that in the event that concentrates or bullion are hauled or shipped by truck to a smelter, market, or mint beyond Cascade, Idaho, there shall be deducted from the net smelter, market, or mint returns the amount for trucking that it would have cost to ship the same by railroad from Cascade, Idaho, to the smelter, market, or mint to which the same are trucked.

“Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.

“It is agreed that reference in this instrument to “Cascade, Idaho”, shall be deemed to include Cascade, McCall, or any nearby place from which shipment is made by rail.”

And that:

“The above covenants on the part of Bradley to pay the royalty herein agreed to be paid shall be considered and held to be covenants running with the lands, grounds, minerals, ores, values, and mining claims hereby conveyed to Bradley and shall be binding upon Bradley, its successors and assigns, forever.”

III.

That said instrument further provides:

“It is agreed that Bradley shall furnish United all necessary information that United may require

to assure it that it is receiving the royalty to which it is entitled hereunder, and that United shall have the right to inspect, examine and make copies of the books and records of Bradley and supporting data at least every six (6) months so as to enable United to satisfy itself that it is receiving its proper royalties." and that:

"In the event Bradley, its successors and assigns, fails or refuses to pay any royalties herein reserved when the same shall become due that the said United shall have a mortgage lien in, to, and upon all of the above and foregoing described properties to secure the payment of said sums and Bradley does hereby mortgage the above and foregoing described properties, and any interest it may hereafter acquire in the Midnight Group hereinafter described, and the whole thereof, to secure the payment of said royalty."

IV.

That at the time said agreement was entered into and thereafter until the commencement of smelter operations upon the mining properties, as herein-after alleged, defendant Bradley Mining Co. mined, extracted and took from said mining properties minerals, ores, metals and values, consisting among others of gold, silver, antimony, tungsten, sulphur, arsenic and copper.

That said Bradley Mining Co. trucked the above mentioned minerals, ores, metals and values from the mining properties to Cascade, Idaho, and there placed the same on railroad for shipment and

shipped the same to smelters or reducing plants in the ownership of which neither plaintiff nor defendant had any interest, and which were located in various parts of the United States.

That said defendant would, monthly, render to plaintiff a statement and copies of smelter settlement statements purporting to show all amounts received by defendant and the defendant would pay to plaintiff the royalty percentage of five per cent (5%) of such amount received by said Bradley Mining Co.

That attached hereto marked Exhibit 2 and made a part hereof as if set forth in full herein is a true, full and correct copy of the statement rendered by the defendant to the plaintiff for the month of December, 1948, being the form of report made by the defendant to the plaintiff prior to the construction of the Yellow Pine smelter.

V.

That in the year 1949 the defendant constructed and began operation of a smelter upon the said mining premises. That said smelter is commonly and hereinafter called the Yellow Pine smelter and the ownership and operation of said smelter by defendant has continued from July, 1949, until the present time and is expected to continue hereafter. That the greater part of the minerals, ores, metals and values extracted from the mining properties are, and since July, 1949, have been, processed through said Yellow Pine smelter. After such processing the saleable products are sold by the said

defendant to various purchasers, the names and addresses of whom are unknown to plaintiff but known to, though undisclosed by, defendant, for sums the amounts of which are unknown to plaintiff but known to, though undisclosed by, defendant at marketing and shipping costs from Cascade, Idaho, known to, but undisclosed by, defendant but unknown to plaintiff.

That notwithstanding the provision in said contract that "the amount paid by any purchaser * * * less marketing and shipping costs from Cascade, Idaho", is the amount upon which the royalty due plaintiff is to be computed and paid by defendant, with respect to sales made by defendant, defendant has, notwithstanding demands of plaintiff therefore, and the hereinbefore quoted provisions of said contract requiring the furnishing of information, refused to furnish the information above alleged to be unknown to plaintiff and to pay royalty based on the amounts paid by such purchasers less marketing and shipping costs.

VI.

That defendant asserts that it interprets said contract so as to permit, with respect to minerals, ores, metals and values passing into the said Yellow Pine smelter, the use of, and it does use, a formula devised by it whereby it purports to allow credits to itself for concentrates passing into said smelter, and to charge against itself deductions, so-called adjusted prices and penalties, for and in respect to the content of said concentrates and to designate

the difference as net smelter returns received by itself from its own said Yellow Pine smelter, and further that said contract permits it to compute and pay to plaintiff as the royalty provided for by said contract five per cent (5%) of said formula determined net smelter returns. That since the commencement of its operation of such smelter it has, and still does, compute and pay royalties in such manner and amounts. That for purposes of illustration of the foregoing there are hereunto annexed, marked Exhibit 3, the report and settlement sheets for the month of March, 1951, upon which defendant has computed and paid royalties, and is typical of the information furnished plaintiff with respect to mined material passing through said smelter and of the method employed by defendant in computing and paying royalties from the beginning of the operation of said smelter to the present.

VII.

That the difference between the amount of royalty computed and paid by the defendant as alleged in Paragraph VI hereof and the amount due plaintiff under the provisions of said contract as alleged in Paragraph V hereof exceeds the sum of \$10,000.00.

VIII.

That as to minerals, ores, metals and values which do not pass through Yellow Pine smelter the practice set forth in Paragraph IV has been and is being followed with respect to reporting and to payment of royalties.

IX.

That an actual controversy exists between the plaintiff and defendant with respect to their rights and other legal relations under said agreement as follows:

1. The provisions of said agreement applicable to the computation and payment of royalties in respect to minerals, ores, metals and values smelted at said Yellow Pine smelter.

2. The nature and extent of the obligation of defendant to furnish to plaintiff information that plaintiff may require to assure it that it is receiving the royalty to which it is entitled.

X.

That this action is between citizens of different States and the amount in controversy exceeds the sum of \$3,000.00, exclusive of interest and costs, and jurisdiction of the Court is conferred by Section 1332, United States Code (Act of June 25, 1948, C. 646, 62 Stat. 930).

Wherefore, Plaintiff prays decree of this Court as follows:

1. That the Court interpret the provisions of said contract exhibit 1, and enter its decree herein determining and decreeing that the proper and legal method for determining the amount of royalty due plaintiff under said contract for minerals, ores, metals and values extracted from said mining claims and smelted at the Yellow Pine smelter of the defendant is by the use of "net revenue" as defined in said contract.

2. That the Court determine and declare that it is the duty of the defendant under said contract to furnish plaintiff the amount paid by purchasers from the sale of minerals, ores, metals and values extracted from said mining claims and smelted at the Yellow Pine smelter and the marketing and shipping costs from Cascade, Idaho.

3. That the Court require an accounting by the defendant to the plaintiff and, upon such accounting being had, that plaintiff have judgment against the defendant for any amount found due, owing and unpaid and that such amount be declared as provided in said contract, a mortgage lien in, to and upon the properties described therein.

4. That plaintiff have such other and further relief as the Court may deem equitable in the premises, and its costs of suit.

SAM S. GRIFFIN,
/s/ SAM S. GRIFFIN,
MAURICE H. GREENE,
/s/ MAURICE H. GREENE,
Attorneys for Plaintiff.

Duly Verified.

EXHIBIT 1

Conveyance, Royalty Agreement and Option

This agreement, made and entered into this 31st day of December, 1941, by and between the United Mercury Mines Company, a corporation, organized and existing under and by virtue of the laws of the State of Idaho, as Party of the First Part, hereinafter called "United", and the Bradley Mining Co.,

Exhibit 1—Continued)

a corporation organized and existing under and by virtue of the laws of the State of California, and authorized to do business in the State of Idaho, as Party of the Second Part, hereinafter called "Bradley".

Witnesseth:

That the said United for and in consideration of the royalty hereinafter agreed to be paid by Bradley, its successors and assigns, to United, its successors and assigns, and in consideration of the mutual covenants and agreements herein contained, and subject to the royalty hereinafter reserved and retained, and the mortgage herein created to secure the payment of said royalty, has granted, bargained, sold, and assigned, and does by these presents grant, bargain, sell and assign, unto Bradley, its successors and assigns, all of the following described lode and placer mining claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, consisting of two groups of lode mining claims, the first of said groups being commonly known as the Meadow Creek Group, and the second of said groups being commonly known as the Hennessy Group, comprising lode and placer claims and comprising the following mining claims, the patents to some of which are of record in the office of the County Recorder of Valley County, State of Idaho, and the Notices of Location of the remainder are of record in the office of the County Recorder of Valley County, State of Idaho, at the Book and Page number herein stated, to-wit:

Exhibit 1—Continued)
Meadow Creek Group

* * * * *

Also the following described mining claims, grounds and lands situate in the Yellow Pine Mining District in Valley County, State of Idaho, the United States Patent for which is recorded in the office of the County Recorder of Valley County, State of Idaho, in Book 3 of Patents at page 172 thereof, and which records are hereby referred to for a more particular description of said claims, to-wit:

* * * * *

Hennessy Group

Together with an easement for a Tailing pond or ponds, and a right of way for a ditch conveying the waters of Sugar Creek through a by-pass, and the right to enter upon the hereinafter described lands for the purpose of diverting the waters of Sugar Creek through a by-pass and maintaining and operating a Tailing pond upon the following described lands situate in Valley County, State of Idaho, to-wit: * * * * *

Together, with all dips, spurs and angles of all lodes located therein;

Together with the tenements, hereditaments and appurtenances and rights and privileges thereunto belonging or in anywise appertaining;

Together with the personal property situate upon said mining claims;

Together with all millsites, power plants, transmission lines, dams, reservoirs, mills, dwellings,

Exhibit 1—Continued)

buildings, structures, water rights, tail races, tailing sites, tailing dams or easements, together with Power Permits Nos. 863 and 1052, and application for Power Permit No. 1857, to have and to hold, subject to the royalty herein reserved and retained by United, all and singular the said premises, together with the appurtenances and privileges thereunto incident, unto the said Bradley, its successors and assigns, forever.

Bradley agrees that it is familiar with the above described mining claims and the conditions of the title it is receiving from United under this instrument, and hereby accepts the same in its present condition, and agrees never to assert any claim against United for or on account of any defects, objections, claims, adverse or otherwise, to the title that United is conveying hereunder. United warrants, however, that it has placed no mortgages upon any of said property that have not been paid, satisfied and discharged, and that it has not sold or assigned said properties, or any part thereof, to any third person, firm or corporation.

For and in consideration of the premises and the conveyance and assignment of the above described properties, Bradley, for itself, its successors and assigns, does hereby covenant, promise and agree to pay to United, its successors and assigns, a royalty of five per cent (5%) on all net smelter returns, net revenue, and net mint returns, as defined herein, upon and for all minerals, ores, metals or values, of any and every kind and character, mined, extracted

Exhibit 1—Continued)

or taken from the above described mining claims, or any part thereof, or from any lands, grounds or claims, lodes or deposits, within the exterior boundaries of said groups of claims; the payment of said five percent (5%) royalty to begin with the first returns received on concentrates shipped from Cascade, Idaho, after Midnight, December 31, 1941, and to continue thereafter for nine hundred and ninety-nine (999) years and as long thereafter as minerals, ores or values shall be extracted, mined or taken from the above described property, at the times and in the manner hereinafter provided; said royalty to be paid to United by depositing the same with the First Security Bank of Idaho, at Boise, Idaho, or at such other place as may be designated in writing by United, to the credit and order of United on or before the 20th day of the calendar month next succeeding the receipt by Bradley of said net returns as defined herein, the same to be so paid each and every month when any net smelter, mint, or other returns are received by Bradley, copies of all sales returns to be furnished United by Bradley.

It is agreed that Bradley shall furnish United all necessary information that United may require to assure it that it is receiving the royalty to which it is entitled hereunder, and that United shall have the right to inspect, examine and make copies of the books and records of Bradley and supporting data at least every six (6) months so as to enable United

Exhibit 1—Continued)

to satisfy itself that it is receiving its proper royalties.

By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho.

By net mint returns, as used herein, is meant the amount paid by any United States Mint, branch or agency thereof, less all shipping and marketing costs from Cascade, Idaho.

It is agreed that in addition to the deductions of railroad freight from Cascade, Idaho, to the smelter, market, or mint, that Bradley shall also be allowed to deduct from the net smelter, market, or mint returns Two Dollars and Fifty Cents (\$2.50) per ton for each ton of concentrates, ores, metals, or values hauled or shipped from the above-described property to Cascade, Idaho, the said sum to be deducted from the net smelter, market or mint returns before net royalty herein provided for is computed.

It is also agreed that in the event that concentrates or bullion are hauled or shipped by truck to

Exhibit 1—Continued)

a smelter, market, or mint beyond Cascade, Idaho, there shall be deducted from the net smelter, market, or mint returns the amount for trucking that it would have cost to ship the same by railroad from Cascade, Idaho, to the smelter, market, or mint to which the same are trucked.

Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.

It is agreed that reference in this instrument to "Cascade, Idaho," shall be deemed to include Cascade, McCall, or any nearby place from which shipment is made by rail.

The above covenants on the part of Bradley to pay the royalty herein agreed to be paid shall be considered and held to be covenants running with the lands, grounds, minerals, ores, values, and mining claims hereby conveyed to Bradley and shall be binding upon Bradley, its successors and assigns, forever.

It is agreed that the time, amount, extent and manner of conducting mining operations and development work upon or in the above-described mining claims shall be in the sole discretion of Bradley, its successors, and assigns, and that the failure of Bradley to mine shall not be held to be a condition subsequent defeating the conveyance made hereby.

Exhibit 1—Continued)

Anything in this agreement contained to the contrary notwithstanding, it is the intention of the Parties to this agreement that the full ownership, possession and control of all the properties above described, and the full ownership, possession and control of all the properties hereinbefore in this instrument conveyed, and all of the personal property acquired and/or used on or in connection with the operation and development of the above described properties, shall be vested in Bradley, and the United shall have no interest in fee in or to said properties, or in and to any of the personal property acquired and/or used in connection with the operation and development of said properties; Except that in the event Bradley, its successors and assigns, fails or refuses to pay any royalties herein reserved when the same shall become due that the said United shall have a mortgage lien in, to, and upon all of the above and foregoing described properties to secure the payment of said sums and Bradley does hereby mortgage the above and foregoing described properties, and any interest it may hereafter acquire in the Midnight Group hereinafter described, and the whole thereof, to secure the payment of said royalty.

It is agreed that three and one-third percent of any sums to be paid by Bradley under the terms of this instrument shall be paid to Oscar W. Worthwine, his heirs or assigns.

For and in consideration of the premises, and the covenant of Bradley to pay the royalty herein-

Exhibit 1—Continued)

before provided for, United hereby gives and grants unto the said Bradley an option to acquire, within one year from December 31, 1941, all the right, title and interest of United in and to that certain group of lode mining claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, commonly known as the Midnight Group, the notices of location of which are of record in the office of the County Recorder of Valley County, State of Idaho, at the Book and Page number herein stated, to-wit:

Midnight Group

* * * * *

Together with all dips, spurs and angles of all lodes located therein;

Together with the tenements, hereditaments and appurtenances and rights and privileges thereunto belonging or in anywise appertaining;

Together with all personal property situate upon said mining claims;

Together with all millsites, power plants, transmission lines, dams, reservoirs, mills, dwellings, buildings, structures, water rights, tail races, tailing sites, tailing dams or easements, To Have and To Hold, subject to the royalty herein reserved and retained by United, all and singular the said premises, together with the appurtenances and privileges thereunto incident, unto the said Bradley, its successors and assigns, forever.

For and in consideration of the premises and the granting of said option upon the Midnight group

Exhibit 1—Continued)

of lode mining claims, Bradley agrees to do the following things:

I.

To do the annual assessment work for the year ending at noon, July 1, 1942, for or upon the above described Midnight group of mining claims, and to do the assessment work for or upon the above described Midnight group of mining claims for the year ending at noon, July 1, 1943, it being understood and agreed that if Bradley does work that can be applied under the laws of the United States as assessment work upon the claims described in the Midnight Group that said work may be performed either upon or for the benefit of said Midnight Group upon other property owned by said Bradley; failure by Bradley to do said assessment work shall not work a forfeiture of the grant and conveyance hereinbefore made.

II.

Bradley further agrees that prior to January 1, 1943, it will examine and test the grounds and lands contained in said Midnight group of mining claims and satisfy itself as to whether it desires to proceed further under the option herein given and granted, the amount and extent of said testing to be in the sole discretion of Bradley.

III.

If said Bradley elects to acquire said Midnight group of mining claims, it shall, on or before the first day of January, 1943, serve written notice to

Exhibit 1—Continued)

that effect upon United by registering a copy of said notice to the United at its office in the Sonna Building, Boise, Idaho, together with a copy thereof to Oscar W. Worthwine, 401 Idaho Building, Boise, Idaho, and a copy of said notice to the First Security Bank of Idaho, at Boise, Idaho; and in addition to serving said notice shall deliver to the said Bank for United the Certificate hereinafter in Paragraph Six (VI) set forth, the same to be duly signed and acknowledged by Bradley.

In the event that Bradley elects not to proceed further under this option, then the said Bradley shall, on or before January 1, 1943, give written notice of its election not to proceed hereunder, the same to be served in the same manner as above provided of its notice of election to proceed hereunder.

IV.

United agrees that upon the execution of this instrument it will deposit a copy of this agreement, together with a mining deed conveying such interest as United may have in the above described Midnight group of mining claims (United not in any way warranting its title) in escrow with the First Security Bank of Idaho, at Boise, Idaho, the same to be delivered by said First Security Bank of Idaho to Bradley upon the receipt by said Bank of the Certificate herein described and upon receipt of the Notice of the election of Bradley to exercise its option to acquire the said Midnight group of lode mining claims under the terms and conditions

Exhibit 1—Continued)

as herein specified, and if Bradley elects not to take said Midnight Group then said deed shall be returned by said Bank to United.

V.

It is agreed that in the event Bradley elects, under this option, to acquire the said Midnight group of lode mining claims and to receive delivery of said deed in escrow with the First Security Bank of Idaho, Boise, Idaho, that thereafter, and beginning as of January 1, 1943, the royalty hereinbefore in this instrument provided for to be paid by Bradley to United shall be increased by one-half ($\frac{1}{2}$) per cent; that is to say, instead of Bradley paying to the said United a five per cent (5%) royalty upon all ores, concentrates and values taken or extracted, marketed, sold or disposed of, from all the properties referred to in this instrument that it shall pay five and one-half ($5\frac{1}{2}\%$) net royalty, as defined herein, upon any and all ores, metals or values extracted, marketed, sold, or disposed of from said Meadow Creek, Hennessy and Midnight Groups of lode mining claims all of which are more particularly described in this instrument, the said five and one-half per cent ($5\frac{1}{2}\%$) royalty, as hereinbefore in this instrument defined, to be paid in the manner and at the times as hereinbefore set forth.

* * * * *

VII.

It is agreed that in the event Bradley elects not

Exhibit 1—Continued)

to acquire said Midnight group of mining claims on or before January 1, 1943, that thereafter, the said Bradley shall have no right, title, interest, or claim in and to the aforesaid Midnight group of mining claims; Provided, However, that the failure of said Bradley to exercise its option as herein given to acquire said Midnight group of mining claims shall in no way affect the conveyance herein made by United to Bradley of said Meadow Creek and Hennessy Groups of mining claims as hereinbefore described, nor shall it in anyway affect the five percent (5%) royalty herein agreed by Bradley *to paid* to said United; and failure to give a written notice of its election not to proceed under this option shall not be considered as an election to proceed under this option.

VIII.

Each party hereto agrees to pay for one-half ($\frac{1}{2}$) the cost of all internal revenue stamps that may be required under this instrument.

IX.

It is agreed that this conveyance and agreement to pay royalties and option agreement settles and adjusts all claims of every kind and character which United has against Bradley, the F. W. Bradley Estate, the Yellow Pine Company, and the Bradley Mining Co., on account of any non-performance by F. W. Bradley, the Yellow Pine Company and/or the Bradley Mining Co.; Except that

Exhibit 1—Continued)

Bradley shall account to United for the royalties that shall be due to United for concentrates shipped by Bradley from Cascade, Idaho, on or before December 31, 1941, and that after Midnight, December 31, 1941, the effective date of this instrument, all other contracts between the Parties hereto shall be held and considered merged in this instrument, and particularly that certain agreement between the Parties hereto entered into upon the 16th day of May, 1939, and acknowledged by the Bradley Mining Co. upon the said 16th day of May, 1939, and by United Mercury Mines Company upon the 24th day of May, 1939, shall be and is hereby merged herein; Except that said last named agreement shall govern the amount of royalties to be paid United for concentrates shipped from Cascade, Idaho, by Bradley on or before December 31, 1941.

X.

It is hereby agreed that the Crocker First National Bank of San Francisco, California, shall return and deliver to the United all deeds heretofore executed by United which it now has in its possession and which are in escrow with said Crocker First National Bank, and that the said Crocker First National Bank is hereby authorized and directed to return all of the deeds to United.

XI.

It is expressly agreed and covenanted that this agreement, and all its terms and conditions, shall

Exhibit 1—Continued)

be forever binding upon the United, its successors and assigns, and upon Bradley, its successors and assigns.

In Witness Whereof, the parties hereto have hereunto set their hands and seals the day and year first above written.

UNITED MERCURY MINES
COMPANY, a corporation,
By J. J. OBERBILLIG,
Its President

Attest: D. D. Oberbillig, Its Ass't Secretary.

BRADLEY MINING CO.,
a corporation,
By JOHN D. BRADLEY,
Its Vice-President

Attest: E. A. Griffen, Its Secretary (Seal).

[Endorsed]: Filed July 12, 1951.

[Title of District Court and Cause.]

ANSWER

Comes now the defendant in the above entitled action and answering plaintiff's complaint on file herein admits, denies and alleges as follows, to-wit:

I.

Defendant denies each and every allegation contained in plaintiff's complaint, except as herein specifically admitted.

II.

Answering Paragraph I of plaintiff's complaint, the defendant admits the allegations contained therein.

III.

Answering Paragraph II of plaintiff's complaint, the defendant admits that on or about December 31, 1941 the plaintiff as first party and the defendant as second party entered into and executed a written conveyance, royalty agreement, and option, a copy of which is annexed to plaintiff's complaint marked Exhibit 1; admits, that, among other things, by said instrument the plaintiff, in consideration of said royalties to be paid by the defendant, conveyed to the defendant numerous mining claims and other property therein described, and that said contract contains among other things, the language quoted therefrom in Paragraph II of said complaint.

IV.

Answering Paragraph III of plaintiff's complaint, the defendant admits that said contract contains, among other things, the language quoted therefrom in Paragraph III of said complaint.

V.

Answering Paragraph IV of said complaint this defendant admits that pursuant to the terms of said agreement this defendant mined, extracted and took from the mining properties minerals, ores, metals and values consisting, among other things, of gold, silver, antimony and tungsten; that prior to the

commencement of the operations of what is commonly called "The Yellow Pine Smelter" the marketable minerals, ores, metals and values were trucked to Cascade, Idaho, and there placed on railroad cars for shipment to smelters or reduction plants located in various parts of the United States and not owned by either plaintiff or defendant; admits that this defendant would monthly render to plaintiff a statement and copies of smelter settlement sheets showing the amounts received by defendant, and admits and alleges that as provided by said agreement defendant paid plaintiff 5% of the amounts received on the sale of such minerals, ores, metals and values whether sold to such independently owned smelters or other reducing plants. Defendant admits that Exhibit 2, attached to plaintiff's complaint, is a true, full and correct copy of the statement so rendered by the defendant to the plaintiff for the month of December, 1948.

VI.

Answering Paragraph V of plaintiff's complaint this defendant admits that in the year 1949 it completed the construction on the mining premises of what is commonly called "The Yellow Pine Smelter," which smelter is the sole property of this defendant; admits that at all times since July, 1949, it has operated and is now operating said smelter and that it hopes to continue such operations hereafter. In this connection defendant alleges that a portion of the concentrates produced from the ores mined from the mining property are now treated in

the Yellow Pine Smelter, but alleges that some concentrates are sold to other smelters; admits that after the smelting process has been completed, certain of the products are sold by this defendant to purchasers, but denies that it has withheld from plaintiff any information relating to the sale of the products so sold and alleges that defendant has made available to plaintiff for inspection tabulations showing all information as to persons to whom such products were sold and the proceeds thereof. Further answering said paragraph this defendant denies that it has refused to pay royalties as required by said agreement and defendant alleges that it has at all times paid all royalties due in accordance with the terms of the agreements of the parties; admits that as to concentrates treated in the Yellow Pine Smelter, it has not computed and paid royalties as demanded by plaintiff and based upon sums received from metal sales, but in this connection alleges there is nothing in the agreement which requires defendant to compute and pay royalties on any such basis.

VII.

Answering Paragraph VI, this defendant denies that it interprets said contract so as to permit it to pay the plaintiff royalties upon a formula devised by it, and alleges that it has at all times since the construction of said Yellow Pine Smelter paid the plaintiff royalties upon all minerals, ores, values and metals passing into said Yellow Pine Smelter upon the basis of net smelter returns as such term

is defined in said agreement. This defendant admits that Exhibit 3 is typical of the information furnished plaintiff with respect to such mined material.

VIII.

Defendant denies Paragraph VII of plaintiff's complaint.

IX.

This defendant admits the allegations of Paragraphs VIII, IX, and X of plaintiff's complaint.

Affirmative Defenses

As affirmative defenses to plaintiff's complaint this defendant alleges:

First Defense

That plaintiff's complaint fails to state a claim against defendant upon which relief can be granted.

Second Defense

1. That following the execution of the agreement of December 31, 1941, referred to in plaintiff's complaint, the defendant, as the owner of the mines and mining property described in said agreement, mined therefrom ores, metals and values, all of which were concentrated on the property, among such ores being ore containing gold, silver and antimony; that the marketable concentrates so obtained were hauled by truck to the rail head at Cascade, Idaho and were then shipped to various custom smelters; that the antimony concentrates were largely shipped to custom smelters located at El Segundo, California, Laredo, Texas and Kellogg,

Idaho, and the gold concentrates shipped to custom smelters located at Midvale, Utah, Tacoma, Washington and elsewhere; that all said smelters were owned by strangers to this proceeding. Defendant alleges that on all concentrates so sold, defendant regularly and in due course paid to the plaintiff five per cent of the net smelter returns, that is to say five per cent of the amount paid defendant for the concentrates so sold after allowance for transportation charges.

2. That in the course of the operation of the mine and the marketing of concentrates it became apparent that to insure continuity of operation of the mine and maximum use of its mineral resources, local reduction of concentrates would be required, both because of the limited and unreliable market for the antimony concentrates produced and because of rapidly increasing costs. As a consequence, the defendant made a study of the advisability of erecting a smelter upon or in the vicinity of the mining property; that after extensive metallurgical studies and the investigation of ore reserves and marketing conditions this defendant determined to erect such smelter; that in 1948 the defendant began the construction of a smelter upon the mining property which it called the "Yellow Pine Smelter" and in July of 1949 began the processing of concentrates therein; that in the operation of the Yellow Pine Smelter defendant has treated all concentrates the principal value of which was antimony, and has treated a substantial portion of the concentrates the principal value of which was gold, and

has continued to sell the remainder of the gold concentrates to outside smelters. Defendant alleges the amount of royalties payable to the plaintiff by the defendant as required by said agreement of December 31, 1941, has been computed as to concentrates treated in the Yellow Pine Smelter upon the basis of net smelter returns as defined in said agreement, which basis is the equivalent of the value of such concentrates on the mining property; that as to concentrates shipped to outside smelters the amount of royalties payable to the plaintiff by the defendant as required by said agreement has been computed upon the basis of the amount paid therefor by the purchaser less transportation charges. This defendant alleges that as a result of the construction and operation of the Yellow Pine Smelter large tonnages of low grade ores have become marketable, which ores, but for the construction of said smelter, would have had little or no value and other ores have become more valuable, and as a consequence plaintiff has been paid and will continue in the future to receive royalty payments far in excess of the royalties that would have been payable had the Yellow Pine Smelter not been constructed.

3. Defendant alleges that the Yellow Pine Smelter was constructed at a cost exceeding Two Million Dollars, all of which cost was borne by the defendant; that since the smelter's completion, the cost of its maintenance and operation has likewise been borne exclusively by the defendant; that nothing contained in said agreement of December 31, 1941, or in any other agreement, obligated the de-

fendant to construct and operate such smelter; that the concentrates which have been and will continue to be smelted in the Yellow Pine Smelter, have a value on the mining property before smelting which value can be determined by price quotations not controlled or influenced by defendant, and that as a consequence the royalty payable to plaintiff can be definitely calculated in money. That plaintiff seeks to so construe the agreement of December 31, 1941 as to require defendant to pay royalty at one percentage of the value of such concentrates if sold to an independently owned smelter and to pay royalty at a higher percentage of the value thereof if the concentrates are processed in the Yellow Pine Smelter; that if so construed said agreement would be unjust and would result in the unlawful taking of the property of this defendant for the benefit of plaintiff and the unjust enrichment of the plaintiff at the expense of this defendant, all in disregard of the clear intent of said agreement.

4. That each month following the execution of the agreement of December 31, 1941, and as required thereby, the defendant has rendered to the plaintiff a full, true and correct statement showing the royalties accrued and payable; that for a long period of time after the execution of the agreement of December 31, 1941, and for a long period of time after the construction and commencement of operations of the Yellow Pine Smelter the plaintiff construed said agreement to entitle it to receive a royalty of five per cent upon net smelter returns irrespective of the ownership or location of the

smelter receiving the concentrates, thus construing and interpreting the language of the agreement in the same manner as the same is now and at all times has been, construed and interpreted by this defendant, and during said period plaintiff accepted without reservation royalty payments so computed; that in an agreement made by the parties dated July 20, 1950, the plaintiff recognized and approved the methods employed by the defendant in computing royalties as being in all respects in strict conformity with the terms and conditions of said agreement of December 31, 1941.

5. That by its complaint in this action, the plaintiff seeks to have the Court so construe said agreement as to disregard the defendant's heavy investment in the Yellow Pine Smelter; to ignore the substantial financial burden and risk assumed by the defendant in constructing and operating said smelter, and particularly to ignore the cost to defendant of reducing concentrates in the Yellow Pine Smelter; to require defendant to pay royalties on such concentrates without deducting normal smelting charges. That such contentions on the part of plaintiff are contrary to the provisions of the agreement; contrary to the interpretation placed thereon by the parties thereto, and would be inequitable and unconscionable.

6. That as the parties well know it was and is the usual custom and practice in the mining and smelting industry to deduct normal smelting charges in computing net smelter returns upon which royalties should be paid; that in accordance with such

custom and practice the parties made the agreement of December 31, 1941; that said agreement (Complaint Exhibit 1—page 8) expressly provides:

“The smelter will deduct its normal smelting charges.”

That by its complaint plaintiff seeks to have the court ignore such express provision of the agreement.

Wherefore, defendant prays that this Court enter a decree as follows:

1. That the plaintiff take nothing by its complaint, and that the defendant have judgment for its costs.

2. That the Court by its decree adjudge and determine that the defendant has computed royalties due the plaintiff in accordance with the terms of the agreement of December 31, 1941, and that defendant will discharge its obligations to plaintiff in the future by computing and paying royalties in accordance with such past practices.

3. That the defendant have such other and further relief as to the Court may seem meet and equitable in the premises.

/s/ RALPH R. BRESHEARS,

/s/ JOHN PARKS DAVIS,

/s/ RAY, QUINNEY & NEBEKER,

/s/ CHENEY, MARR, WILKINS &

CANNON,

Attorneys for Defendant

Duly Verified.

Acknowledgment of Service attached.

[Endorsed]: Filed September 14, 1951.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above entitled action came on regularly for trial upon the 19th day of March, 1957, before the above entitled Court, sitting without a jury, at Boise, Idaho. The plaintiff appeared by and through its attorneys of record, E. H. Casterlin, Paul S. Boyd, and Dale Clemons; and the defendant appeared by and through its attorneys of record, John Parks Davis, Paul H. Ray, Robert E. Brown, G. A. Marr, and Ralph R. Breshears.

Whereupon documentary evidence was introduced and admitted, and one witness on the part and behalf of the defendant was sworn and examined and the evidence being closed said cause was duly submitted to the Court for its consideration and decision and having duly considered the evidence and the oral arguments of the parties to said action, the Court, being now fully advised both in the law and in the premises, hereby makes the following Findings of Facts and Conclusions of Law, constituting its decision in writing herein, and hereby finds the facts to be as follows:

Findings of Fact

I.

That the plaintiff is a corporation organized un-

der the laws of the State of Idaho, doing business therein, and is a citizen of that State, and that the defendant is a corporation organized under the laws of the State of California, licensed to do business in Idaho, and is a citizen of the State of California.

That the amount in controversy exceeds, exclusive of interest and costs, the sum of \$3000.00.

II.

That the plaintiff was, on and before December 31, 1941, the owner of two groups of lode and placer mining claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, commonly known as the Meadow Creek Group and the Hennessy Group, more particularly described in Defendant's Exhibit 7, Plaintiff's Exhibit 23.

III.

That on December 31, 1941, the plaintiff and defendant entered into a written "Conveyance, Royalty Agreement and Option", whereby the plaintiff bargained, sold and assigned the Meadow Creek Group and the Hennessy Group of lode and placer mining claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, as more particularly described in Defendant's Exhibit 7, Plaintiff's Exhibit 23, to the defendant, subject to the agreement on the part of the defendant to pay the plaintiff a royalty, as in said "Conveyance, Royalty Agreement and Option" provided.

IV.

That upon the execution of said "Conveyance, Royalty Agreement and Option" the defendant became and now is the owner of the Meadow Creek and Hennessy Groups of placer and lode mining claims, described in said agreement, subject to the terms and conditions of said agreement, together with all minerals, ores, metals and values contained therein.

V.

That for and in consideration of the conveyance and assignment by the plaintiff to the defendant of the Meadow Creek and Hennessy Groups of placer and lode mining claims, the defendant agreed to pay to the plaintiff a royalty of five per cent on all net smelter returns, net revenue, and net mint returns, as defined in the "Conveyance, Royalty Agreement and Option", upon and for all minerals, ores, metals or values of any and every kind and character, mined, extracted or taken from said mining claims, said agreement providing with respect thereto as follows:

"For and in consideration of the premises and the conveyance and assignment of the above described properties, Bradley, for itself, its successors and assigns, does hereby covenant, promise and agree to pay to United, its successors and assigns, a royalty of five per cent (5%) on all net smelter returns, net revenue, and net mint returns, as defined herein, upon and for all minerals, ores, metals

or values, of any and every kind and character, mined, extracted or taken from the above described mining claims, or any part thereof, or from any lands, grounds or claims, lodes or deposits, within the exterior boundaries of said groups of claims; the payment of said five per cent (5%) royalty to begin with the first returns received on concentrates shipped from Cascade, Idaho, after Midnight, December 31, 1941, and to continue thereafter for nine hundred and ninety-nine (999) years and as long thereafter as minerals, ores or values shall be extracted, mined or taken from the above described property, at the times and in the manner hereinafter provided: * * * ”

“By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

“By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho.

“By net mint returns, as used herein, is meant the amount paid by any United States Mint, Branch or agency thereof, less all shipping and marketing costs from Cascade, Idaho.

“It is agreed that in addition to the deductions of railroad freight from Cascade, Idaho, to the smelter, market or mint, that Bradley shall also be allowed to deduct from the net smelter, market, or mint returns Two Dollars and Fifty Cents (\$2.50) per ton for each ton of concentrates, ores, metals, or values hauled or shipped from the above-described property to Cascade, Idaho, the said sum to be deducted from the net smelter, market or mint returns before net royalty herein provided for is computed.

“It is also agreed that in the event that concentrates or bullion are hauled or shipped by truck to a smelter, market, or mint beyond Cascade, Idaho, there shall be deducted from the net smelter, market, or mint returns the amount for trucking that it would have cost to ship the same by railroad from Cascade, Idaho, to the smelter, market, or mint to which the same are tracked.

“Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.

“It is agreed that reference in this instrument to ‘Cascade, Idaho,’ shall be deemed to include Cascade, McCall, or any nearby place from which shipment is made by rail.

“The above covenants on the part of Bradley to pay the royalty herein agreed to be paid shall be considered and held to be covenants running with the lands, grounds, minerals, ores, values, and mining claims hereby conveyed to Bradley and shall be binding upon Bradley, its successors and assigns, forever.

“It is agreed that the time, amount, extent and manner of conducting mining operations and development work upon or in the above-described mining claims shall be in the sole discretion of Bradley, its successors, and assigns, and that the failure of Bradley to mine shall not be held to be a condition subsequent defeating the conveyance made hereby.”

VI.

That pursuant to said contract defendant mined, extracted and took from the mining properties, minerals, ores, metals and values consisting, among other things, of gold, silver, antimony and tungsten, and prior to commencement of operations of “The Yellow Pine Smelter” the marketable minerals, ores, metals and values were trucked to Cascade, Idaho, and there placed on railroad cars for shipment to smelters or reduction plants located in various parts of the United States not owned by either plaintiff or defendant, and in which neither party had any interest; that monthly statements were rendered by defendant to plaintiff with copies of smelter settlement sheets showing amounts received by defendant; and that defendant paid plaintiff

five per cent (5%) of the amounts received by defendant on the sale of such minerals, ores, metals and values; and that Exhibit 2 attached to plaintiff's Complaint (Plaintiff's Exhibit 24 herein) is a true copy of the statement rendered by defendant to plaintiff for the month of December, 1948.

That the same practice continued after July 1949 with respect to all shipments to smelters in which neither Bradley nor United had any interest.

VII.

That in 1949 defendant completed the construction on the mining premises of "The Yellow Pine Smelter", at a cost in excess of Two Million Dollars, solely owned by defendant; that defendant operated said smelter and at the time of the commencement of this action was operating said smelter; that the cost of maintaining and operating said smelter has been borne exclusively by the defendant; that fifty-five (55%) per cent of the concentrates produced from the ores mined from the property were treated in The Yellow Pine Smelter and after completion of the smelting process certain of the products were sold by defendant to purchasers; that as to concentrates treated in the Yellow Pine Smelter defendant has not computed and paid royalties as demanded by plaintiff, in that as to concentrates treated at the Yellow Pine Smelter on the premises, defendant has not computed and paid royalties based upon sums received by it from sales of products resulting from the smelting process.

VIII.

That exhibit 3 attached to plaintiff's complaint (Plaintiff's Exhibit 25 herein) is typical of the information furnished by defendant to plaintiff with respect to mined material passing through the Yellow Pine Smelter.

That defendant Bradley has paid plaintiff United royalty upon minerals, ores, metals and values passing into the Yellow Pine Smelter based upon net smelter returns in the manner typified by Exhibit 3, attached to the complaint (Plaintiff's Exhibit 25 herein).

IX.

That an actual controversy exists between the plaintiff and defendant with respect to their rights and other legal relations under said agreements as follows:

1. The provisions of said agreement applicable to the computation and payment of royalties in respect to minerals, ores, metals and values smelted at said Yellow Pine Smelter.

2. The nature and extent of the obligation of defendant to furnish to plaintiff information that plaintiff may require to assure it that it is receiving the royalty to which it is entitled.

X.

That the defendant completed construction of the Yellow Pine Smelter at its own costs and charges upon the mining claims during the year 1949 and

went into operation during July, 1949, and it has at all times been its sole property.

XI.

That the salable products resulting from concentrates processed at The Yellow Pine Smelter are held and retained by the Bradley Mining Company as its sole property until the same are sold to a purchaser.

XII.

That Bradley Mining Company has sold to purchasers salable products resulting from the smelting and reduction of minerals, ores, concentrates, metals and values from the said mining claims and smelted in the Yellow Pine Smelter.

XIII.

That from and after receipt by defendant of the net smelter returns from concentrates shipped to outside smelters defendant had no right, title or interest in or to such concentrates, the same being the property of said outside smelters.

XIV.

That the defendant has sold to purchasers salable products resulting from the smelting and reduction of minerals, ores, metals and values taken from the said mining claims and smelted in The Yellow Pine Smelter.

XV.

That defendant has not paid plaintiff sums equal to five per cent (5%) of the amount paid to de-

defendant by purchasers of products resulting from defendant's Yellow Pine Smelter operations.

XVI.

That the books and records of defendant correctly show the amount received by defendant as net smelter returns on all concentrates shipped to independent smelters.

XVII.

That the books and records of defendant correctly show that the royalties payable to the plaintiff on net smelter returns received by defendant, Bradley Mining Company, from independent smelters have been paid to the plaintiff.

XVIII.

That at the time of the execution of the contract, December 31, 1941, there were no smelters located at Cascade, Idaho.

XIX.

That the net smelter returns provisions of the "Conveyance, Royalty Agreement and Option" dated December 31, 1941, is applicable to the operations of the defendant at the Yellow Pine Smelter for ores, concentrates, metals and values taken from the claims described in the agreement, and the charges and deductions made by the defendant for smelting ores at the Yellow Pine Smelter have been proper and settlements made by the defendant have been correct as to the minerals, ores, metals and values processed at the smelter. That the defendant has paid to the plaintiff all royalties due it under

said agreement for or on account of any ores, concentrates, metals or values taken from the mining claims described in said contract and processed at the Yellow Pine Smelter.

XX.

That there is no dispute as to the meaning and interpretation of the "net mint return" clause of the contract.

XXI.

That before 1939 and thereafter at all times material to this action, it was the practice and custom in the smelting industry for companies who own and operate smelters also to own and operate mines; that it was likewise the practice and custom in the industry for companies owning mines and also owning smelters to ship their mine products to their own smelters; that it was likewise the practice and custom of owners of smelters and mines also to lease mining properties from other independent owners and send the products extracted therefrom to their own smelters and to settle for the products so shipped on the same basis as such smelting companies would settle with independent or custom shippers; that it was a practice and custom of the trade that where ores treated came from the mines owned by the owners of smelters, or came from mines leased and mined by the smelter owners, or came from independent custom shippers, that the smelting charges and the cost of transportation of concentrates to the smelter were deducted to arrive

at a net amount commonly referred to in the mining and smelting industries at "net smelter returns."

XXII.

That it is a matter of common knowledge and historically recognized in the mining industry that the milling of ores to reduce such ores to a concentrate form is a part of the mining process and that the smelting of ores is not a part of the mining process.

XXIII.

Tax problems were discussed during the negotiation of the 1941 agreement, including the problem of depletion, and the parties contracted with respect to these problems and with reference to existing laws. Section 114 (b) (4), B, U. S. Internal Revenue Code of 1939, made provision for depletion allowances computed upon the gross income from the property, and the statute defined the gross income from the property to mean the gross income from mining; and the definition of the term "mining" as contained in that section of the U. S. Internal Revenue Code, includes the ordinary treatment processes, which, according to the universal usage and custom in the mining industry are considered to be a part of mining, and excludes from the definition of "mining" additional process for purification and treatment of ores and minerals such as roasting, thermal or electric smelting, and refining.

XXIV.

That at the time negotiations were initiated be-

tween plaintiff and defendant for the purpose of consummating the "Conveyance, Royalty Agreement and Option" dated December 31, 1941, (Defendant's Exhibit 7, Plaintiff's Exhibit 23), the plaintiff owned the mining property covered by the agreement of December 31, 1941, and the defendant was operating it under an Option to Purchase, dated May 16, 1939 (Defendant's Exhibit 5), by the terms of which the defendant was required to pay the plaintiff a royalty, on a schedule graduated upward from seven and one-half per cent ($7\frac{1}{2}\%$) to ten per cent (10%) and then to twelve and one-half per cent ($12\frac{1}{2}\%$) of all net smelter or net mint returns or net revenues as defined in the Option Agreement, on all concentrates, metals, ores and values extracted from the optioned mining claims; said Option Agreement providing in this respect as follows:

"The Optionee hereby agrees * * *

"(c) To pay to the Optionor, at the time and in the manner hereinafter provided, the following royalties upon all ores, metals or values extracted from the mining grounds included in this option during the periods hereinafter named;

First: For the period from August 1st, 1939, and ending at midnight, July 31st, 1944, a royalty of seven and one-half per cent ($7\frac{1}{2}\%$) upon all net smelter, or mint returns, or net revenues, as defined herein, on all concentrates, metals, ores and values extracted from said optioned mining claims;

Second: For the period beginning August 1st, 1944, and ending at midnight, July 31st, 1949, a

royalty of ten per cent (10%) upon all net smelter, or mint returns, or net revenues as defined herein on all concentrates, metals, ores and values extracted from said optioned mining claims;

Third: For the period beginning August 1st, 1949, and thereafter, a royalty of twelve and one-half per cent (12½%) upon all net smelter, or mint returns, or net revenues, as defined herein, on all concentrates, metals, ores and values extracted from said optioned mining claims."

"The said royalties shall be deposited by Optionee in the Crocker First National Bank of San Francisco, California, to and for the credit and order of said Optionor, on or before the twentieth (20th) day of the calendar months next succeeding the receipt of said net returns by Optionee, and the same to be so paid each and every month when there are any net smelter or mint or other returns until the purchase price of said mining claims and properties has been completed as herein provided. It is agreed that concentrates cannot be hauled from the property during the late fall, winter and early spring months, and that the time when the same shall be shipped during the summer months shall be determined by Optionee. It is understood, however, that should local reduction of the concentrates become practicable as determined by the Optionee, that no concentrates will be shipped."

"By net smelter returns, as used herein, is meant the amount received from the smelter from any ores, concentrates, metals, or values shipped to a smelter, it being understood that the smelter will deduct its

normal smelting charges, and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

“By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped less marketing and shipping costs from Cascade, Idaho.

By net mint returns, as used herein, is meant the amount paid by any United States Mint, branch or agency thereof, less all shipping and marketing costs from Cascade, Idaho.”

XXV.

That said “Option Agreement” dated May 16, 1939 (Defendant’s Exhibit 5) was prepared by plaintiff’s attorney, O. W. Worthwine, an experienced mining attorney, and during the negotiations preceding the execution of said “Option Agreement” plaintiff’s attorney submitted a rough draft of certain pages of the proposed “Option Agreement” (Defendant’s Exhibit 5a) to Mr. John D. Bradley, Executive Vice President of defendant Bradley Mining Company, which said rough draft (Defendant’s Exhibit 5a) contained a definition of “net mill returns” to be used in connection with the computation of royalties payable to the plaintiff; and that Mr. Bradley crossed out the definition of “net mill returns”, for the reason that the defendant had other mineral products that were not covered by the “net mint” or “net smelter” clauses, because, as Mr. Bradley stated, the term “net milling” was not as broad as “net revenue” and would not cover

actual mercury processing and their might be high grade ore that would not be milled. That Mr. Bradley, after crossing out the definition of "net mill returns" as it appeared on Exhibit 5a, when first submitted to him, inserted in lieu thereof in his own handwriting, the definition of "net revenue" as the same appears in the "Option Agreement" of May 16, 1939, as executed by the plaintiff and defendant. And Mr. Bradley likewise inserted in the definition of "net smelter returns", in his own handwriting, after the word "received", the words "from the smelter"; and before the words "smelting charges" he inserted the word "normal"; and added to the last line of the definition, following the word "smelter", the words "shall also be deducted"; which changes, as made by Mr. Bradley, were incorporated in the "Option Agreement" of May 16, 1939, as executed by the defendant and plaintiff.

XXVI.

That the purpose that the plaintiff and defendant had in setting or putting aside the "Option Agreement" dated May 16, 1939, (Defendant's Exhibit 5) and substituting therefor the "Conveyance, Royalty Agreement and Option", dated December 31, 1941 (Defendant's Exhibit 7, Plaintiff's Exhibit 23), and the economic reasons for negotiating and executing the agreement of December 31, 1941, were as follows:

a. The purpose of the defendant was to obtain a reduction in the amount of royalties required to be paid by the defendant to the plaintiff;

b. The purpose of the plaintiff, in agreeing to lower royalties in accordance with and as provided in the 1941 agreement, was to induce the defendant to carry on more intensive mining operations on the property and make it economically feasible and attractive for the defendant to mine low-grade ore.

XXVII.

That a construction of the "Conveyance, Royalty Agreement and Option" dated December 31, 1941 (Defendant's Exhibit 7, Plaintiff's Exhibit 23), which would not entitle or permit the defendant to deduct its normal smelting charges before computing royalties on the products of the mining property processed and smelted at the Yellow Pine Smelter, would result in a substantial increase in the amount of royalty over that which would be payable if the defendant is entitled to compute the royalties payable to plaintiff on ores produced from defendant's property and processed at the Yellow Pine Smelter on the basis of "net smelter returns"; and that in itself would be a construction contrary to the purpose of the contract and contrary to plaintiff's avowed purpose at the time the contract was executed.

XXVIII.

That during the negotiations which led up to the execution of the "Conveyance, Royalty Agreement and Option" dated December 31, 1941 (Defendant's Exhibit 7, Plaintiff's Exhibit 23), the possibility that the defendant might build a smelter at the site of the mine was discussed and both plaintiff and

defendant contemplated that the defendant might erect a smelter at the site of the mine; and in that contemplation the parties inserted in the contract the following provision:

“Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.”

XXIX.

That at the time of the negotiation and execution of the “Conveyance, Royalty Agreement and Option”, dated December 31, 1941, (Defendant’s Exhibit 7, Plaintiff’s Exhibit 23) tungsten had been discovered upon the mining property. Substantial quantities of tungsten were shipped from the mining property during the fall of 1941. Tungsten ore was mined and taken from the property during the years 1941, 1942, 1943, 1944 and into the year 1945, and became the most important part of the mining operation in the history of the mine from beginning to end; and through all those years the defendant continued to treat tungsten ore mined from the property and send it direct to purchasers other than smelters. At the time the contract of 1941 was consummated, there was no custom or practice in the mining industry to send tungsten ore to a smelter.

XXX.

During the period that the defendant was mining

and selling tungsten ore direct from the mine to purchasers, defendant made reports of all such sales to the plaintiff and paid royalty to the plaintiff on the proceeds of such sales, computed on the basis of the "net revenue" clause contained in the contract.

XXXI.

Smelting, as commonly known and understood in the mining industry, consists of roasting, reduction and refining; and in the mining industry the heat treatment of quicksilver at the mine is not considered as smelting.

XXXII.

During the time that the defendant was producing tungsten on the mining property, the mining of other minerals increased and the mining property had a greater production of antimony.

XXXIII.

That crude ore, such as antimony and gold extracted from a mine in its native state with impurities, is first put through a mill or concentrator as a part of the mining process. The processing of concentrates at a smelter adds value to them, and is the final preparation of the product of the mine for the market. Processing and treatment of concentrates at a smelter is not known or considered in the mining industry as a part of mining; and it is the custom and practice in the industry for smelters, in purchasing antimony concentrates, to pay one-half of the gross value of the metal content in the concentrates.

XXXIV.

The plaintiff and defendant, having in mind that the "Conveyance, Royalty Agreement and Option", dated December 31, 1941 (Defendant's Exhibit 7, Plaintiff's Exhibit 23), was to last for an unusually long period of time, envisioned not only present possible methods of marketing the current mine product from the property, but also the possible variety of minerals which possibly would be produced and marketed in the future, including gold, silver, antimony, tungsten and quicksilver. The emphasis in the contract upon market returns indicates, in the light of all of the other circumstances, that the parties had in mind all possible marketing methods. That as to any product that could go directly from the mine to the mint, the mint was the market. That as to any product of the mine required to go to a smelter, the smelter was the market. That as to other products of the mine, the "net revenue" provision was intended as a catch-all, another method of marketing direct from the property; and the provisions of the contract for the computation and payment of royalties by the defendant on the basis of "net revenue" and the definition of "net revenue", as contained in the contract, were carried over from the Option Agreement of May 16, 1939 (Defendant's Exhibit 5) and incorporated in the 1941 agreement, for the purpose of providing a basis for computing and paying royalties on all products of the mine that did not require processing at a smelter other than those marketed directly to the mint; and in particular to

provide a basis for computing and paying royalties on the sales of tungsten sold directly from the mine to the market and not to a smelter.

XXXV.

That the plaintiff's construction of the 1941 contract, that is: that the defendant is not entitled to and does not have the right to deduct normal smelting charges before computing royalties upon products of the mine processed at the Yellow Pine Smelter, and that the plaintiff is entitled to a royalty upon the proceeds from the sales of all products of the mine after processing by the defendant at the Yellow Pine Smelter, would read out of the definition of "net smelter returns" as contained in the contract, the phrase

"* * * it being understood that the smelter will deduct its normal smelting charges * * *"

or it would necessarily read into the definition the words "third party owned smelter" or "outside smelter".

XXXVI.

That the "Conveyance, Royalty Agreement and Option" dated December 31, 1941 (Defendant's Exhibit 7, Plaintiff's Exhibit 23) was drafted by O. W. Worthwine, acting as attorney for the plaintiff. John Parks Davis represented the defendant as its attorney, and the contract was made by experienced mining people, including Mr. Worthwine, the principal draftsman, and a party interested in the contract; and the parties contracted with reference to the practices and customs in the mining

industry prevailing at that time and as they envisioned such might be over the years.

XXXVII.

That in 1943 the defendant constructed a purification plant at Boise, Idaho, known as the "Boise Purification Plant", for the purpose of treating and further purifying some of the tungsten extracted from the mining property, by removing phosphorus, antimony, sulphur, arsenic, and other impurities, before shipping it to market. The Boise Purification Plant was operated by the defendant for approximately two and one-half years, and during all of that period the defendant computed and paid royalties to the plaintiff on the proceeds of all sales of tungsten processed and treated at the Boise Purification Plant after deducting from the proceeds of such sales, operating costs, including depreciation; and submitted reports to the plaintiff each month with complete information as to all such sales, and deductions made by the defendant for operating costs and depreciation, as typified, by copy of invoice of tungsten shipment from Boise Purification Plant to Sylvania Electric Products Company dated May 23, 1945, with settlement sheet attached, dated July 14, 1945, showing deduction of operating costs, including depreciation (Plaintiff's Exhibit 29); and the plaintiff did not at any time make any objection to this method of settlement, or protest to the defendant about its right to deduct operating costs and depreciation before computing

royalties upon the sale of tungsten, after treatment in the Boise Purification Plant.

XXXVIII.

The treatment by the defendant of tungsten at the Boise Purification Plant added value to the mined product and would not be considered in the mining industry as a part of mining, as that term is known in the industry; and the method of settlement by the defendant with the plaintiff with respect to the computation and payment of royalties payable upon tungsten treated and processed at the Boise Purification Plant was under the "net smelter returns" provisions of the contract.

XXXIX

The plaintiff did not reply to letter from John D. Bradley, Executive Vice President of Bradley Mining Company to John J. Oberbillig, President of United Mercury Mines Company dated March 31, 1948 (Defendant's Exhibit 32), which contained the following statements and proposals:

"As Harold Bailey and I explained to you on March 12, 1948 in your office, we are planning on erecting at Stibnite a smelter for the local reduction of our antimony concentrates — our present plans also include locally reducing our gold concentrates in the future."

"Although I am positive that you fully appreciate the importance of such a move, still I am listing below the benefits of a smelter to the Yellow Pine Mining District as we see them at present."

"Upgrading of marginal ore bodies owing to

greater metal recoveries and payments will add longer life to the Yellow Pine Mine. At the present time we have approximately $11\frac{1}{2}$ million tons of low-grade antimony-gold ore which can only be made profitable with a local smelter—undoubtedly, large additional tonnages of this type of material will be developed as we continue our drilling and other exploration program.”

“Under the present program of shipping raw concentrates, there is no pay for gold and silver in the antimony concentrates; and in the instances of the gold concentrates, there is little and sometimes no pay for the antimony contained in these concentrates—this situation will be corrected by the smelter installation.”

“According to the present Bradley Mining Co.-United Mercury Mines Co. contract, “normal smelting charges are to be deducted in arriving at “net smelter returns”. “Normal smelter charges”, as you know, are comprised not only of treatment charges but also metal and quotational gains. In fact, in the case of our antimony shipments the “normal smelting charges” are entirely quotational gains.”

“I believe you will agree with us that to arrive at “normal smelting charges” for our several different types of concentrates in the case of a local smelter can prove most complex over the ensuing years. Accordingly, I am proposing a simplified procedure for locally reduced concentrates—such procedure to be equivalent to the royalty you now receive on the present 5% basis when it is applied to the shipment of raw concentrates.”

“Although the following calculations show a variance for the equivalent royalty in the instance of sales of locally reduced products from 2.30% to 2.50% we have proposed that the rate for such products be set of 2.75%.”; and plaintiff did not make any objection or other response to any of the statements and proposals contained in said letter.

XL.

That on the 20th day of July, 1950, plaintiff and defendant entered into an agreement in writing modifying the terms of the contract of December 31, 1941, which agreement (Defendant’s Exhibit 6) was drafted by O. W. Worthwine as attorney for the plaintiff, and which agreement contains the following recitals:

“Whereas, the said Bradley Mining Co., did, on the 20th day of June, 1950, pay to the United Mercury Mines Company and said Oscar W. Worthwine the royalties due for the month of May, 1950;” * * *

“It is further agreed that the said Bradley Mining Co. shall make the usual monthly reports as to moneys received by it during the preceding month upon which royalties would be payable, stating the amounts of royalties that had accrued, but, instead of sending the check as has been the practice during the past ten years, shall make a notation thereon to the effect that ‘the above accrued royalty has been postponed for a period of one (1) year from theday of....., 1950, to the day of, 1951, at which time the same shall become payable’.”

And the evidence is uncontradicted that the royalty paid to the plaintiff upon products of the mine treated by the defendant at the Yellow Pine Smelter for the month of May, 1950, were computed and paid according to the "net smelter returns" method provided for by the contract of December 31, 1941. (Defendant's Exhibit 7, Plaintiff's Exhibit 23.)

XLI.

That the defendant has computed and paid royalties to the plaintiff upon products of the mine treated and processed by the defendant at the Yellow Pine Smelter on the same basis and utilizing the same treatment schedule, but without deducting freight charges, as in the case of identical concentrates shipped to outside smelters; the net effect being that plaintiff benefited in royalty payments when identical concentrates were smelted by the defendant at the Yellow Pine Smelter as compared with the best arrangement that could be made with an independently owned smelter; and the plaintiff did not object to the payment of such royalties by the defendant upon the basis of "net smelter returns" until 1951.

Conclusions of Law

As Conclusions of Law from the foregoing Findings of Fact, the Court hereby finds and concludes:

I.

That the Court has jurisdiction of the parties and of the subject matter of the action.

II.

That the proper and legal method for determining the amount of royalty due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941, for minerals, ores, metals and values extracted from the mining claims described therein and smelted by the Yellow Pine Smelter of the defendant is by the use of the "net smelter returns" provision as defined in the contract; and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of salable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by the defendant at the Yellow Pine Smelter.

III.

That the defendant does not, as of March 21, 1957, owe plaintiff anything by way of royalties, or otherwise, for or on account of any ores, concentrates, metals or values taken from the mining claims described in said contract and processed at the Yellow Pine Smelter.

IV.

That it is the duty of the defendant, under the terms of said contract, to furnish plaintiff information as to the amount paid by purchasers from the sale of minerals, ores, metals and values extracted from said mining claims and smelted at the Yellow Pine Smelter, and the marketing and shipping costs from Cascade, Idaho.

V.

That it is the duty of the defendant, and that the defendant be required, to furnish plaintiff all necessary information that it may require to enable it to determine that it is receiving the royalty to which it is entitled under the terms of said contract, and that the plaintiff have the right to inspect, examine and make copies of the books, records, and supporting data of the defendant, at least every six months, so as to enable plaintiff to determine that it is receiving the royalty to which it is entitled.

VI.

That each party shall bear its own costs.

It Is Hereby Ordered That a judgment be entered herein accordingly.

Dated this 20th day of April, 1957.

/s/ WM. C. MATHES,

Judge of the United States
District Court.

[Endorsed]: Filed April 5, 1957.

It Is Ordered, Adjudged and Decreed:

I.

That the proper and legal method for determining the amount of royalty due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941, for minerals, ores, metals and values extracted from the mining claims described therein and smelted at the Yellow Pine Smelter of the defendant, is by the use of the "net smelter returns" provision as defined in the contract; and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of salable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by the defendant at the Yellow Pine Smelter.

II.

That the defendant is not indebted to the plaintiff, and the plaintiff is not entitled to recover from the defendant, as of March 21, 1957, any money by way of royalty, or otherwise, for or on account of any ores, concentrates, metals or values taken from the mining claims described in said "Conveyance, Royalty Agreement and Option" and processed at the Yellow Pine Smelter.

III.

That the defendant be, and it hereby is, required to furnish plaintiff with the amount paid by purchasers from the sale of minerals, ores, metals and

values extracted from said mining claims and smelted at the Yellow Pine Smelter, and the marketing and shipping costs from Cascade, Idaho.

IV.

That the defendant be, and it hereby is, required to furnish plaintiff all necessary information that it may require to enable it to determine that it is receiving the royalty to which it is entitled under the terms of said contract; and that the plaintiff shall have the right to inspect, examine and make copies of the books, records and supporting data of the defendant at least every six months, so as to enable plaintiff to determine that it is receiving the royalty to which it is entitled.

It Is Further Ordered, Adjudged and Decreed That each party to this action shall bear its own costs.

Dated this 20th day of April, 1957.

/s/ WM. C. MATHES,
Judge of the United States
District Court.

[Endorsed]: Lodged April 5, 1957. Filed April 24, 1957.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that United Mercury Mines Company, a corporation, plaintiff above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in this action on April 24th, 1957.

/s/ PAUL S. BOYD, by D. C.,
P. O. Box 2084, Boise, Idaho,

/s/ E. H. CASTERLIN,
P. O. Box 1384, Pocatello, Idaho,

/s/ DALE CLEMONS,
Idaho Building, Boise, Idaho,
Attorneys for Plaintiff.

[Endorsed]: Filed May 20, 1957.

[Title of District Court and Cause.]

UNDERTAKING FOR COSTS

Whereas, the plaintiff in the above entitled action is about to appeal to the United States Court of Appeals for the Ninth Circuit, from a Judgment, Case No. 2854, entered against the plaintiff in said action, in said United States District Court, Southern Division, State of Idaho, in favor of Defendant in said action on the 24th day of April, 1957.

Now, Therefore, in consideration of the premises, the United States Fidelity & Guaranty Company of

Maryland, a corporation organized and existing under the laws of the State of Maryland, and authorized to transact Surety business in the State of Idaho, does hereby undertake and promise to pay such costs and charges as may be awarded against the plaintiff by judgment, or in the progress of said action, not exceeding the sum of Three Hundred and no/100 Dollars (\$300.00), to which amount the United States Fidelity & Guaranty Company of Maryland acknowledges itself bound.

Dated this 20th day of May, 1957.

THE UNITED STATES FIDELITY & GUARANTY CO.,

/s/ By

Attorney-in-Fact,

Countersigned:

.....

Agent at Boise, Idaho.

[Endorsed]: Filed May 20, 1957.

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

To the Clerk of the above entitled Court:—

Pursuant to Rule 75(a) of the Federal Rules of Civil Procedure the Plaintiff-Appellant hereby designates the entire and complete record and proceedings in the above entitled matter for inclusion in the record on appeal in this action taken by the

Notice of Appeal filed herein on the 20th day of May, 1957.

/s/ PAUL S. BOYD, by D. C.,
P. O. Box 2034, Boise, Idaho,
/s/ E. H. CASTERLIN,
P. O. Box 1384, Pocatello, Idaho,
/s/ DALE CLEMONS,
Idaho Building, Boise, Idaho,
Attorneys for Plaintiff-Appellant.

Acknowledgment of Service Attached.

[Endorsed]: Filed May 20, 1957.

[Title of District Court and Cause.]

REPORTER'S PRAECIPE

To G. C. Vaughan, Official Reporter,—

Will you please prepare, certify and lodge a Reporter's transcript of the proceedings had in the above entitled Court on March 19th, 1957, pursuant to the rules of the Court.

We agree to pay the charges therefor.

/s/ PAUL S. BOYD, by D. C.,
P. O. Box 2084, Boise, Idaho,
/s/ E. H. CASTERLIN,
P. O. Box 1384, Pocatello, Idaho,
/s/ DALE CLEMONS,
Idaho Building, Boise, Idaho,
Attorneys for Plaintiff-Appellant.

Acknowledgment of Service attached.

[Endorsed]: Filed May 20, 1957.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

United States of America,
District of Idaho—ss.

I, Ed. M. Bryan, Clerk of the United States District Court for the District of Idaho, do hereby certify the foregoing papers to be the complete original record filed in this office in the above entitled case:

1. Complaint.
2. Motion for Enlargement of Time to Plead.
3. Stipulation Enlarging Time to Plead.
4. Order Approving Stipulation and Enlarging Time to Plead.
5. Answer.
6. Motion to Strike.
7. Notice of Motion for Summary Judgment.
8. Motion for Summary Judgment.
9. Motion to Strike Portions of Affidavit in Support of Summary Judgment.
10. Minutes of the court of November 29, 1951.
11. Affidavit of John D. Bradley.
12. Affidavit of Harold E. Lee.
13. Acknowledgment of Service.
14. Motion to Strike Portions of Affidavit of Harold E. Lee.
15. Affidavit of John J. Oberbillig.
16. Stipulation to withdraw certain sentences from affidavit of John J. Oberbillig.
17. Minutes of the court of Feb. 25, 1952.
18. Minutes of the court of Sep. 5, 1952.

19. Withdrawal of Attorney Maurice H. Greene.
20. Minutes of the court of Oct. 10, 1952.
21. Memorandum Opinion of Judge Healy.
22. Request for Admissions.
23. Defendant's Response to Request for Admissions.
24. Interrogatories by Plaintiff.
25. Notice of Hearing Objections to Interrogatories.
26. Defendant's Answers to Plaintiff's Interrogatories.
27. Defendant's Objections to Certain Interrogatories.
28. Motion for Production, Inspection and Copying.
29. Motion for Protective Order Limiting Scope of Order for Production, etc.
30. Notice of Hearing Motion for Protective Order, etc.
31. Order to submit Objections on briefs and argument.
32. Order to submit Motion to limit scope upon briefs, etc.
33. Memorandum Decision of Judge Healy.
34. Defendant's Answers to Plaintiff's Interrogatories.
35. Plaintiff's Request for Admissions.
36. Request for Admissions under Rule No. 36.
37. Response to Request for Admissions.
38. Response to Request for Admissions under Rule No. 36.
39. Minutes of the court of Feb. 1, 1955.

40. Judgment.
41. Notice of Appeal.
42. Cost Bond.
43. Designation of Contents of Record on Appeal.
44. Reporter's Transcript.
45. Praecipe for Reporter's Transcript.
46. Statement of Points.
47. Mandate from the United States Court of Appeals.
48. Satisfaction of Judgment for Costs.
49. Interrogatories by Plaintiff.
50. Notice of Hearing Objections to Interrogatories, with Objections attached.
51. Defendant's Answer to Plaintiff's Interrogatories.
52. Praecipe for Appearance of Robert E. Brown as an attorney for the defendant.
53. Notice of Motion to Produce.
54. Motion to Produce.
55. Minutes of the Court of Aug. 17, 1956.
56. Stipulation for Taking of deposition of John J. Oberbillig.
57. Order to remove Stipulation and attach same to deposition of John J. Oberbillig.
58. Minutes of the court of Feb. 19, 1957.
59. Reporter's Transcript of Pre-Trial Conference.
60. Pre-Trial Conference Order.
61. Minutes of the Court of March 19, 1957.
62. Minutes of the Court of March 20, 1957.
63. Minutes of the Court of March 21, 1957.

64. Affidavit of Service of Proposed Findings of Fact and Conclusions of Law, and Judgment.

65. Findings of Fact and Conclusions of Law.

66. Judgment.

67. Notice of Appeal.

68. Undertaking for Costs.

69. Designation of Record on Appeal.

70. Reporter's Praecipe.

71. Order Extending Time for docketing appeal.

72. Reporter's Transcript (Judge's opinion of 3/21/57 included).

73. Original Exhibits.

(4) Agreement dated 10/3/30 (Admitted as excluded evidence).

(5) Option Agreement—May 16, 1939.

(5-a) Draft of proposed contract.

(6) Agreement dated 7/20/50.

(7) Agreement dated 12/31/41 (Attached to original Complaint).

(11) Copy of letter dated 4/14/48.

(21) Original letter dated 12/30/41 (Admitted as excluded evidence).

(22) Original letter dated 12/30/41 (Admitted as excluded evidence).

(23) Agreement dated 12/31/41 (On page 12 of Transcript of Record of former appeal. Same as Exhibit 7).

(24) 5 pages of Exhibit 2 attached to original Complaint (Also on pages 27, 28, 29, 30 and 31 of Transcript of Record of former appeal).

(25) Part of Exhibit 3 attached to original Com-

plaint (Also on pages 32 to 40 of Transcript of Record of former appeal).

(26) Plaintiff's Request for Admissions (Page 179 of Transcript of Record of former appeal).

(26-a) Response to Request for Admissions (Page 184 of Transcript of Record of former appeal).

(27) Interrogatories by plaintiff (Page 149 of Transcript of Record of former appeal).

(27-a) Defendant's Answer to Plaintiff's Interrogatories (Page 151 of Transcript of Record of former appeal).

(27-b) Defendant's Answers to Plaintiff's Interrogatories (Page 166 of Transcript of Record of former appeal).

(28) Request for Admission 2(q) (Page 145 of Transcript of Record of former appeal).

(28-a) Response to Request for Admission 2(q) (Page 148 of Transcript of Record of former appeal).

(29) Copy invoice of shipment of Tungsten dated 5/23/45.

(30) Pre-Trial Conference Order filed March 11, 1957. (With original file.)

(31) Letter dated 12/2/48.

(32) Letter dated 3/31/48.

In witness whereof I have hereunto set my hand and affixed the seal of said court this 25th day of July, 1957.

[Seal] /s/ ED M. BRYAN,
Clerk.

In the United States District Court for the District
of Idaho, Southern Division

No. 2854

UNITED MERCURY MINES COMPANY, a
Corporation, Plaintiff,

vs.

BRADLEY MINING COMPANY, a Corporation,
Defendant.

TRANSCRIPT OF PROCEEDINGS

This matter came on for hearing before the Honorable William C. Mathes, United States District Judge, sitting without a jury, at Boise, Idaho, on March 19, 1957.

Appearances: E. H. Casterlin, Esq., Pocatello, Idaho, Paul S. Boyd, Esq., Boise, Idaho, Dale Clemons, Esq., Boise, Idaho, Attorneys for the Plaintiff. John Parks Davis, Esq., San Francisco, California, Paul H. Ray, Esq., Salt Lake City, Utah, G. A. Marr, Esq., Salt Lake City, Utah, Robert E. Brown, Esq., Kellogg, Idaho, Ralph R. Breashears, Esq., Boise, Idaho, Attorneys for the Defendant. [1]*

March 19, 1957

10:00 O'Clock A.M.

Mr. Casterlin: May we inquire if the Pre-trial Order, as prepared and sent down, has been signed?

* Page numbers appearing at bottom of page of Reporter's Transcript of Record.

The Court: Yes, I should have said it has been signed as presented. I made one or two purely typographical corrections, or corrections of typographical errors. They are so minor that I don't even find them now. I think I recall that one was where I simply added an "s".

Mr. Casterlin: Could that be on Page Six, your Honor, near the end of Paragraph L, I notice one letter has been deleted. It is at the top of the page, in the third line.

The Court: No, I missed that one, that word is obviously meant to be mining. I had in mind that I had made one or two minor corrections, but I don't see them. I had in mind that there was some word that should have been plural and it was singular, and I put an "s" at the end of it. Here it is, it is at the bottom of Page Thirteen, it read "The foregoing admission of fact" and I figured that should be admissions, that is the change that I made. There is one matter that I perhaps should mention at this juncture, and that is referred to under Paragraph Q on Page Six, and that reads, in the Pre-trial Order, "That, if under the terms [3] of the contract, Defendant, Bradley Mining Company, is entitled to make any charge or deduction for smelting ores in the Yellow Pine Smelter, the charges and deductions so made by Bradley Mining Company have been proper charges and deductions and all settlements made with the plaintiff have been correct." As I read that it means that if any smelter charges at all were deducted, which have been deducted by the defendant, cover-

ing the smelting of ores in the Yellow Pine Smelter, have been reasonable and necessary and there is no issue as to the smelter charges as such.

Mr. Boyd: At this time, if the Court please, we desire to move, or rather we desire to have the record show, in order to protect ourselves,—there appears to be some difference of understanding between counsel—my understanding is that we have to save all objections as to relevancy, materiality and competency here throughout the entire record, except those matters that are specifically stipulated, and that you reserve all other objections as to materiality.

Mr. Casterlin: Yes, everything is reserved except what is waived.

The Court: That is covered by Paragraph b or sub-paragraph b in Paragraph IV at the top of Page Eight. [4]

Mr. Boyd: In Paragraph Q on Page Six, we have included the words “have been proper charges and deductions”, and we have taken the position that these records apply only to the charges that were proper and that were properly reported to us,—as to materials reported to us, and not as to any other material or any other product here that has not been reported, or course, we are not stipulating to that as we have no knowledge.

The Court: Is there any that has not been reported?

Mr. Boyd: I do not know, and neither does co-counsel, we have talked to our client and he doesn't know. However, if there is something that

comes up we would not want to be foreclosed from going into the matter.

The Court: But as to any ore with respect to which there has been some report following the smelter process, you accept the smelter charges by the Plaintiff, do you,—the charges made by the Defendant against the Plaintiffs?

Mr. Boyd: As far as reported, that is exactly as we have it in our Stipulation.

The Court: And the result would be, as I see it, if the contract is interpreted in the way the Defendant contends, namely, that the smelter returns are all covered, then the Judgment will be [5] for the Defendant without any recovery at all by the Plaintiff.

Mr. Boyd: But we still have the accounting.

The Court: Then Paragraph Q only covers, shall I say, the rate of smelter charges, is that it? In other words, the charge that the defendant has made for smelting was a reasonable and necessary charge, is that the purport of Paragraph Q?

Mr. Casterlin: I think that Paragraph Q, as far as this discussion is concerned, provides that the charges, so far as reported, are correct, but if there is anything not reported, anything that we have no knowledge of, we are not saying as to the correctness of that.

The Court: To put it another way, whatever charges the defendant has deducted on the reports heretofore made, for smelting charges, are stipulated to be reasonable, necessary and proper.

Mr. Casterlin: Yes, so far as reported.

Mr. Breshears: Now, your Honor, I would like to say something on that. That question was raised for the first time when we came to consider the final draft of this Pre-trial Order. If your Honor will remember, the Court discussed this matter quite at length with counsel at the time of the Pre-trial Conference, and it is specifically [6] stipulated in the record of the Pre-trial Conference that if it is ultimately determined that our theory is correct, that we are entitled, or required to pay royalties only on net smelter returns, that all settlements that have been made are correct without qualification, and that stipulation is in the record.

The Court: I don't understand that the Plaintiff seeks to depart from that at all. He merely takes the position, as I understand it here now, that if there are any ores that have been smelted on which no report has been made, they have not seen the deductions for the smelting charges and therefore they cannot say whether they are reasonable, but I assume that if they are at the same rate as those which the Defendant reported and proved then the Plaintiff would be bound by it as being a reasonable and necessary rate.

Mr. Breshears: My understanding from conferences with them was that they were not conceding that everything was reported by Bradley that went into that smelter, and the purpose of the Stipulation was to eliminate any question of accounting as to what went through the smelter, and they have had some six years to determine whether or not Bradley reported everything, and there is an Order

in the files authorizing them to examine our books.

The Court: Is there any contention by the Plaintiff, and is it the contention now, that there have been ores go through the smelter upon which there have been no reports to the Plaintiff?

Mr. Casterlin: It is our position that we don't know.

The Court: You want to reserve it as a precautionary reservation that proof might develop something, is that it?

Mr. Casterlin: Yes, but there is no hedging on the settlement so far as the settlement sheets are concerned that have been submitted.

The Court: I don't think that this is anything that we need to take any time with, Gentlemen. It is my own view that if some such matters should develop and the same rate or smelting charge was applied to that, then the Plaintiff would be bound as to the reasonableness and necessity of that charge, otherwise, if something should develop that has not been reported then the Court would be inclined to release the Plaintiff from the stipulation. Literally, however, Q might foreclose the Plaintiff.

Mr. Breshears: I think they are foreclosed by the Stipulation on Page 45 of the record.

The Court: That may be so, but if the proof should show that there have been ores go through [8] that smelter upon which there was no accounting, then the Court would be inclined to relieve the Plaintiff from the Stipulation, but, as I understand it now, there is no contention that there were any. Does the Plaintiff have any further

proof to offer besides the Pre-trial Conference Order?

Mr. Casterlin: I understand that we have reservation upon everything that has not been waived.

The Court: As it stands now, does the Plaintiff wish to offer in evidence any admissions in the Pre-trial Conference Order?

Mr. Casterlin: Yes.

The Court: Do you wish to offer in evidence all of the admissions in the Pre-trial Conference Order?

Mr. Casterlin: Yes.

The Court: Do you wish to offer in evidence the entire Pre-trial Conference Order?

Mr. Casterlin: I think possibly I misunderstood your Honor, no, the Pre-trial Order stands in the record by itself, so as to the admissions in there we do not intend to encumber the record with any evidence or any documents whatsoever.

The Court: Then does the Plaintiff have any evidence to offer further? [9]

Mr. Casterlin: We will call Mr. Bryan, the Clerk, with the original files.

ED. M. BRYAN

Called as a witness by the Plaintiff, after being first duly sworn, testifies as follows:

Direct Examination

Q. (By Mr. Casterlin): Will you state your name for the record? A. Ed. M. Bryan.

Q. You are the Clerk of this Court?

(Testimony of Ed. M. Bryan.)

A. Yes, sir.

Q. Do you have with you the original files in the case which is now pending? A. Yes, sir.

Q. Will you identify the Complaint, if you please?

A. The Complaint was filed on July 12, 1951.

Mr. Casterlin: We now offer in evidence Exhibit 1, which is attached to the Complaint, which is the contract of December 31, 1941.

The Court: As amended by interlineation.

Mr. Casterlin: As amended by interlineation.

The Court: It may be admitted.

Mr. Bryan: Your Honor, we usually mark [10] these exhibits consecutively and I was wondering if we could mark this as Plaintiff's Exhibit Number 23, since we have 22 exhibits by the Defendant.

The Court: Is there any objection to that?

Mr. Casterlin: No sir, none.

The Court: Then it is so ordered, this will be exhibit number 23. The contract isn't listed in the exhibits, is that right?

Mr. Casterlin: No.

The Court: Isn't it Exhibit Number 7?

Mr. Brown: Defendant's Exhibit 7?

The Court: It is listed in the Pre-trial Conference Order, and I wonder if there is any objection to marking it as Exhibit Number 7 here?

Mr. Casterlin: No objection to that.

The Court: Then we finally have it marked correctly as Exhibit Number 7 in evidence, that is the

December 31st, 1941 contract, the contract in controversy.

[Note: Exhibit No. 7 is the same as Exhibit No. 1 set out at pages 12-26 of this printed record.]

Mr. Casterlin: We now offer in evidence Exhibit Number 2 attached to the Complaint, which is a sample monthly statement settlement sheets.

The Court: Is that marked in the Pre-trial Conference Order? [11]

Mr. Casterlin: No, it is not, your Honor, and I suggest that be marked as Exhibit Number 24, Plaintiff's Exhibit 24.

The Court: I believe that is mentioned somewhere in the Pre-trial Conference Order, isn't it?

Mr. Boyd: Would that be under 4 E?

Mr. Brown: Yes, I think that's right.

Mr. Casterlin: That is an agreement that the exhibit is typical, that is all that is referred to there.

The Court: Then if it is not marked, it may be Exhibit Number 24 in evidence.

Mr. Ray: May I inquire how many sheets there are to that exhibit.

The Court: Is that the same as Exhibit 2 attached to the Complaint?

Mr. Casterlin: Exhibit 7 is the same as Exhibit 1.

The Court: And Exhibit 24, last received, is the same as Exhibit 2, to the Complaint. As I understand it, Mr. Ray is inquiring as to how many sheets comprise Exhibit Number 24. [12]

Mr. Casterlin: These exhibits all appear in the transcript of the Circuit Court of Appeals Opinion.

Mr. Ray: We have no objection to Exhibit Number 24.

The Court: Very well. The Clerk advises that there are twelve sheets comprising Exhibit Number 24.

Mr. Ray: The reason I inquired of that was that I thought he was referring to the material reproduced in the Transcript of the Record of the Circuit Court of Appeals, there are many sheets but I believe five of them in this record are identified as Exhibit Number 2.

The Court: The Clerk states that the figure twelve was a misapprehension on his part, and now he wants to make a count of the number.

Mr. Casterlin: It is apparent now, if the Court please, that in printing the Circuit Court record we did not print all of Exhibit 2, I will now, with consent of counsel, limit Exhibit Number 2 to the exhibit as printed in the Transcript of the Circuit Court, which eliminated a good many of these pages.

The Court: Do you have an extra copy of that record that the Clerk may have?

Mr. Casterlin: Yes, there is an extra copy. [13]

The Court: And I understand this is on Page 27 of the record?

Mr. Casterlin: Page 27.

The Court: Then the five sheets that appear following Page 27 of the record of the Transcript of the Court of Appeals of the Ninth Circuit shall

comprise Exhibit Number 24 in evidence here in lieu of the large number of pages that appears in Exhibit 2 attached to the Complaint.

Mr. Casterlin: I will offer it in that way.

Mr. Ray: And we have no objection.

The Court: Very well, it may be received.

Mr. Casterlin: We now offer as Exhibit Number 25 what is designated as Exhibit Number 3 attached to the Complaint. The same appearing in the Transcript of the record of the Circuit Court of Appeals at Page 32 to 40, inclusive. The same being a sample statement from the Bradley Mining Company to the United, and illustrative of the computation of royalties on concentrates smelted at the Yellow Pine smelter.

Mr. Ray: It seems to me that the material you refer to also are settlement sheets of other smelters.

Mr. Casterlin: Which were submitted by [14] Bradley to the United.

Mr. Ray: We have no objection.

The Court: As I understand it, this is offered as being an exemplar or typical of the report of the information furnished by the defendant to the plaintiff with respect to mined material passing through the Yellow Pine smelter.

Mr. Casterlin: That is correct.

The Court: There being no objection it may be received in evidence. Is that the same as Exhibit 3 in the Complaint?

Mr. Casterlin: Yes, limited, however, to certain pages.

The Court: Such portions as appear in the Transcript on appeal.

Mr. Casterlin: Yes.

The Court: Very well, and that is designated as Exhibit Number 25 here.

Mr. Casterlin: I now offer Plaintiff's Requests for Admission, which was filed October 15, 1954, and which appears in the Transcript of the record of the Circuit Court of Appeals on Page 179.

The Court: Do the answers appear as a part of that document?

Mr. Casterlin: No, your Honor, these are [15] just the requests.

The Court: Is there any objection?

Mr. Ray: No objection.

The Court: It may be received as Exhibit 26.

Mr. Casterlin: We now offer in evidence the answers to the same requests, which were filed November 2, 1954, and which appear in the Transcript at Page 184,—the Transcript of the record of the Court of Appeals.

The Court: If there is no objection it will be received as Exhibit 26A.

Mr. Casterlin: In this connection, if Counsel please, these two letters to which reference is made in the request are copies, and they are signed by J. D. B. in both instances, referring to Page 179, 180, of the record, which is a letter dated January 29, 1942, to Mr. George K. Dorsey from J. D. B. Is there any question as to J. D. B. is?

Mr. Ray: There is no question as to that, Mr. Casterlin, J. D. B. is John D. Bradley.

Mr. Casterlin: And at the time he was President of the Bradley Mining Company, was he?

Mr. Ray: At what time is that?

Mr. Casterlin: On January 29, 1942. [16]

Mr. Ray: He was at that time Executive Vice-President.

Mr. Casterlin: Executive Vice-President.

The Court: And is that so stipulated by both parties?

Mr. Casterlin: Yes, we accept that. Now then, referring to Page 181 of the Transcript and the letter dated March 17, 1947, addressed to Mr. John J. Oberbillig, and signed John D. Bradley, Executive Vice-President, there is no question about his official capacity with the Bradley Mining Company at that time, I take it.

Mr. Ray: No, none.

Mr. Casterlin: Now then, Counsel, these Requests for Admission and Answers set forth copies of the letters, do you insist that we furnish copies of these Exhibits or that the copies in the Requests and the Answers may serve for that purpose?

Mr. Ray: We would not require you to furnish us additional copies if we have them, Mr. Casterlin.

Mr. Casterlin: The admission is that the letters are genuine, I was just trying to avoid encumbering the record. [17]

Mr. Ray: And with the offer of these, we reserve the objection to their relevancy, we still have that reservation.

Mr. Casterlin: Yes, that is understood.

The Court: Now, if they come in as a part of

the Requests for Admissions and the Answers thereto, perhaps we should rule on those objections now. I have received the Requests for Admissions as Exhibit Number 26, and you now talk about objections, is there any objection to that Exhibit, to those Requests?

Mr. Ray: To the introduction of the Requests?

The Court: Yes.

Mr. Ray: No, there is none.

The Court: Now then, let me inquire, are the letters attached to the Requests?

Mr. Casterlin: Yes.

The Court: And is there any objection to the Answers which have been received as Exhibit 26A. As I would interpret it, the receipt of the Requests would bring in the documents attached.

Mr. Ray: You are now talking about the letters on Page 180?

Mr. Casterlin: Yes.

Mr. Ray: We don't object to that. [18]

The Court: Very well. Then the Requests, Exhibit 26, and the Answers, Exhibit 26A, are in evidence with all of the Exhibits thereto attached.

[See page 398.]

Mr. Casterlin: We now offer in evidence Plaintiff's Interrogatories filed November 2, 1953, which appear in the Transcript at Page 149, and that is offered as Exhibit Number 27.

The Court: Plaintiff's Interrogatories filed November 2, 1953?

Mr. Casterlin: Yes.

The Court: Is there any objection?

Mr. Ray: No objection.

The Court: That is received in evidence as Exhibit Number 27.

[See page 399.]

Mr. Casterlin: We now offer as Plaintiff's Exhibit Number 27A, the Defendant's Answers to the same Interrogatories, filed November 10, 1953, which appear in the record of the Circuit Court at Page 151.

Mr. Ray: We have no objection.

The Court: Received in evidence as Plaintiff's Exhibit 27A.

[See page 401.]

Mr. Casterlin: We now offer in evidence as Exhibit Number 27B, which are the Defendant's Answers to the same Interrogatories——

The Court: ——Further answers? [19]

Mr. Casterlin: Yes. Filed on May the 17th, 1954, and appear in the record of the Circuit Court at Page 166.

The Court: Is there any objection to the further Answers?

Mr. Casterlin: The fact is that when we submitted the Interrogatories they answered some and objected to others, and these further Answers are the answers to the ones that they objected to in the first place.

Mr. Ray: No, we don't object.

The Court: The further Answers, last identified as Exhibit 27B, are received in evidence.

[See page 404.]

Mr. Bryan: May I interrupt, please?

The Court: Yes, you may.

Mr. Bryan: According to the record, this record, Defendant's Answers were filed November 2, 1953, instead of November 10, that is Exhibit 27A.

The Court: According to my note, Exhibit 27, Plaintiff's Interrogatories were filed November 2, 1953, and the Answers wouldn't likely be filed the same day.

Mr. Bryan: There is just a month difference, your Honor. One was October 2nd and the other November 2nd.

The Court: The Interrogatories, Exhibit 27, were filed October 2? [20]

Mr. Bryan: Yes sir, according to this, I am looking at the Transcript.

The Court: And that is what you are going by, is it, Gentlemen, the Transcript?

Mr. Casterlin: That's right.

The Court: Then Exhibit 27A, the Answers, were filed a month later, November 2.

Mr. Casterlin: Yes, that seems to be correct.

The Court: And Exhibit 27B, further Answers, were filed May 17, 1954.

Mr. Bryan: That is correct, according to this.

The Court: Now, go ahead with the next, Mr. Casterlin.

Mr. Casterlin: Now, if the Court please, I offer in evidence Requests for Admission Q,—Subdivision Q, filed September 17, 1953, which appears at Page 145 of the Transcript.

The Court: Plaintiff's Request Q, is that it?

Mr. Casterlin: Yes.

The Court: Just the single request?

Mr. Casterlin: Yes, just the single request. [21]

The Court: Is there any objection?

Mr. Ray: No objection.

The Court: That would be Exhibit 28, would it, Mr. Casterlin?

Mr. Casterlin: Yes, Exhibit 28.

The Court: Exhibit 28 is received in evidence.

[See page 408.]

Mr. Casterlin: We now offer in evidence Defendant's Response to the Request, which appears on Page 148 of the Transcript, under Subdivision request number two, Q.

The Court: Do you have the date of filing on that?

Mr. Casterlin: Filed October 2, 1953.

The Court: Is there any objection to that Exhibit, to the Response?

Mr. Ray: We do not object to it.

The Court: Very well, received in evidence as Exhibit 28A.

[See page 413.]

Mr. Casterlin: The Plaintiff rests.

The Court: You may proceed, Gentlemen, on behalf of the Defendants.

Mr. Ray: We would like to have Mr. John D. Bradley sworn. [22]

JOHN DAVIS BRADLEY

Called as a witness by the defendant, after being first duly sworn, testifies as follows:

Direct Examination

Q. (By Mr. Ray): Did you give your name, Mr. Bradley? A. Yes sir, I did.

Q. Where do you live?

A. My residence is Burlingame, California.

Q. What connection have you with the defendant, Bradley Mining Company?

A. I am an Executive Vice President of the Bradley Mining Company.

Q. Presently are you associated with any other mining company?

A. Yes, the Bunker Hill Company.

Q. What is the Bunker Hill Company?

A. The Bunker Hill Company is a lead and zinc mining and smelting company.

Q. Where does it operate?

A. It operates in northern Idaho.

Q. What is your connection with the Bunker Hill Company?

A. I am President of the Bunker Hill Company.

Q. According to the correspondence now in the record there is reference to F. W. or Fred Bradley. Who was he? A. He was my father. [23]

Q. What was his business?

A. His business was mining.

Q. How old are you, Mr. Bradley?

A. I am 46.

(Testimony of John Davis Bradley.)

Q. What was your first contact with mining, Mr. Bradley, and where was it?

A. I think my first contact was probably at the age of six or seven that I can recollect. I don't know how far back you want to go, Mr. Ray.

Q. Have you been associated more or less with mining ever since your early childhood?

A. Yes, I have.

Q. When did you first perform any work in and around mining?

A. At the age of thirteen.

Q. Where was that?

A. At The Spanish Mine near Grass Valley, California.

Q. And what was the nature of that mine?

A. That was a gold mine.

Q. Were you working there during vacation?

A. Yes.

Q. Vacation from school?

A. Yes, I worked there during the summer and Christmas vacations.

Q. And did you ultimately enter a mining school? A. Yes.

Q. Where was that? [24]

A. The School of Mines at the University of California.

Q. What was your course of study?

A. Mining engineering.

Q. Were you graduated from that school?

A. Yes, in 1933 with a B.S. in Mining Engineering.

(Testimony of John Davis Bradley.)

Q. In 1933? A. Yes.

Q. And following your graduation——

Mr. Casterlin: ——We will admit the witness' qualification as a mining engineer.

Mr. Ray: I am glad to know that and to accept that offer, but I do want to show his relation with mining and mines and with the mining customs that followed.

The Court: Can it be stipulated that he is a qualified mining engineer, and not only that, but that he is familiar with the custom and practices of mining in the State of Idaho?

Mr. Casterlin: Yes, we will admit that with the reservation that the custom in the mining industry is immaterial in this case, on the authority of the Idaho cases, and further that the custom and practice is not an issue in this case, and thirdly, that the custom and practice does not become important in any event until it is first established that the [25] contract is uncertain, ambiguous and unintelligible.

The Court: Now, is it stipulated that this witness was familiar with the custom and the practices in the mining industry in Idaho during the period of the formation of the contract in suit here? Perhaps the period can be fixed, I will ask this. During what period have you been familiar with the custom and practice?

Mr. Ray: That is what I would like to follow up.

The Court: Perhaps we would save time—let

(Testimony of John Davis Bradley.)

me ask again, what period have you been familiar with the custom and practices of the mining industry in the State of Idaho?

A. In the early thirties.

The Court: Since the early 1930's?

A. Yes sir.

The Court: Will the plaintiff so stipulate?

Mr. Casterlin: Yes.

Q. (By Mr. Ray): In connection with the mining industry, following your graduation from college, where did you work?

A. I worked in North Idaho and also in Grass Valley.

Q. What were the products produced in the Grass Valley property? [26]

A. We produced gold in a concentrate form and also in bullion form. In other words, we had an oxidized ore which we cyanided and recovered the gold, and we also had a sulfadized ore where, in addition to recovering the gold and silver, we recovered zinc.

Q. How was the gold disposed of, the bullion?

A. The bullion was sold to the mint.

Q. During what years was that, Mr. Bradley, the middle thirties?

A. Yes, the middle thirties.

Q. So, you became familiar at that time with the sale of bullion produced at the Grass Valley Mine to the mint?

A. That's right. We also produced a crude barite at this property.

(Testimony of John Davis Bradley.)

Q. You mentioned gold concentrates, gold bullion and barite, how did you dispose of the concentrates?

A. The gold concentrates were sold to the American Smelting and Refining Company plant at Selby, California.

Q. And how were you paid for that?

A. On the basis of net smelter returns.

Q. Now, was the barite shipped to a smelter?

A. No.

Q. How was it disposed of?

A. It was sold in its crude form, and sold to one of the National Lead Company subsidiaries near Modesto. [27]

Q. So that you had material set forth there that was sold on a mint basis, on a net smelter return basis, and on a mixed? A. Correct.

Q. The barite was shipped and settled for neither on a mint returns nor net smelter returns?

A. That is correct.

Q. Now then, Mr. Bradley, where else, before you became active in the mining industry in Idaho, did you pursue mining in California?

A. Well, in my younger days I was familiar with tungsten mining in the Mojave Desert, but from an executive or a management standpoint, it was more limited to the Spanish Mine near Grass Valley, the San Juan Mine near Grass Valley, which was a direct shipping mine, we didn't concentrate, and then in the quicksilver mines in California, Oregon and Nevada.

(Testimony of John Davis Bradley.)

Mr. Casterlin: May I inquire, if the Court please, if this testimony is offered for the purpose of qualifying the witness as to his experience?

Mr. Ray: It is offered for that purpose and for the additional reason that we understand that the case is here and the principal issue for the Court to decide is what the parties meant by this contract, and the evidence is offered so that we may, as nearly as possible, place the Court in the situation that the parties were in when they made the contract, and that includes the background, [28] the mineral knowledge and mining knowledge of the parties.

The Court: It would not be the subjective position, it would be the objective would it not, it would be the intention of both parties and not the intention of just one.

Mr. Ray: That is right, your Honor, but we can't get it all at one time.

Mr. Casterlin: If it is offered for that purpose, I think I will make the objection that it is incompetent, irrelevant and immaterial for any purpose whatsoever until it is first established that the contract in question, which is up for interpretation, is uncertain, ambiguous, and unintelligible, and requires interpretation as to its meaning.

The Court: I have ruled that the contract requires interpretation, it doesn't take much to require interpretation as I understand it, but I haven't ruled on this specific problem.

Mr. Casterlin: Is it the Court's position,—and

(Testimony of John Davis Bradley.)

this is to clarify it in my own mind,—is it the Court's position that the question here is the ambiguity of the language of the contract or the uncertainty of the application of the clear, plain and simple language as to the operation of the Yellow Pine smelter.

The Court: It may be both. [29] Judge Healey interpreted the contract one way and Judge Denman and his associates appeared to take a different view, in any event, however the situation may be with respect to the ambiguity of the language as such, the so-called royalty as applied to the situation which developed, namely, following the construction of the Yellow Pine smelter, as applied to that, the contract is ambiguous.

Mr. Casterlin: The contention here, as I understand it, is whether the language of the contract, which is clear, plan and defined by agreement of the parties, is applicable to the Yellow Pine smelter.

The Court: I don't know whether I can subscribe to that portion, that it is clear, plain and defined, as you say, but I will rule that it applies and would apply to a situation comparable here, namely, what payments were to be made by the defendant for the product of this mine that has been run through the Yellow Pine smelter. The contract is not clear, it is ambiguous, but even if that situation didn't exist, if there was a dispute between the parties as to the meaning of the contract I would rule that the circumstances surround-

(Testimony of John Davis Bradley.)

ing the execution would be admissible to aid in the interpretation because of the dispute, even though the Court might think that there was no ambiguity at all.

Mr. Casterlin: I will agree with the Court's [30] statement, so far there hasn't appeared any uncertainty between the parties as to the definition of the terms in the contract, which they have placed on those terms by their own language.

The Court: As to the meaning of the contract, as to the royalty provision, shall I say, as applied to the products put through the Yellow Pine smelter, that would be admissible.

Mr. Casterlin: I understand that there is no dispute as to the clarity of the terms as to what net revenue means, as to what net smelter returns means, and what net mint returns means, because the parties, by agreement, have defined them.

The Court: As far as this witness' background is concerned, it is relevant, only in the issue as to his qualifications as an expert. His background and experience would be relevant as to that, but I should not say that it would be relevant to any of the issues involved here, except as it might affect his qualifications to testify as an expert.

Mr. Casterlin: That is the reason I inquired as to the purpose of this line of questioning and answers.

The Court: The record shows the admission by counsel of his qualifications, but for all the [31] record shows now the practice and custom in min-

(Testimony of John Davis Bradley.)

ing in California and Nevada might be entirely different than the practice and customs in Idaho.

Mr. Casterlin: I am leading up to the decision in the Utah Construction Company case where it is held that where there is no uncertainty or ambiguity there is no room for interpretation based on matters outside of the contract, or for importing extraneous matters in aid of interpretation.

The Court: Of course, in passing on these questions, the Court gets involved in the same problems of semantics that the parties themselves do.

Mr. Casterlin: From a semantic standpoint the parties themselves have defined the meaning of the terms in clear language.

The Court: The parties have attempted to define those terms all right, but whether it is clear or not, I don't need to pass on that at the moment.

Mr. Casterlin: That is the reason I wanted to ask this question as to what was the purpose, whether it was applied to the application of the contract as to the operation of the Yellow Pine smelter.

Mr. Ray: To get to the point of this clause in the contract, I would like to show, and I will show, if I am permitted, how it came about, what [32] connection Mr. Bradley had with this and what background he had at the time that he did what he did, and the discussion that he had with the other side about it.

The Court: It seems to me that it would not be relevant to show that he disposed of the product

(Testimony of John Davis Bradley.)

of a mine in three different ways or methods, down in California.

Mr. Ray: But, your Honor, I can't prove the area of the custom of all of those things all at once.

The Court: Then perhaps you should tell us your purpose, do you propose to show that these customs and practices prevailed in Idaho at the time of the formation of this contract?

Mr. Ray: Yes, your Honor.

The Court: Very well, the objection will be overruled.

Mr. Casterlin: Then, your Honor, I think it is incompetent, irrelevant and immaterial to show what the custom was or is in California if the same custom prevailed in the State of Idaho at the Stibnite property.

The Court: Your objection I take it, could, if it was made to the form of the question, the issue here is not what his experience has been, the issue is what is the custom and practice in the mining [33] industry, what was the custom and usage in the industry, even though he may not have participated personally in any of them, I take it that he is an expert on it and he would be competent to testify. So as far as his personal experiences are concerned, if his qualifications are admitted, I will sustain the objection. Are his qualifications admitted?

Mr. Casterlin: Yes sir.

Mr. Ray: With respect to smelting and mining?

(Testimony of John Davis Bradley.)

The Court: I have accepted the statement that his qualifications are admitted entirely. If there are any objections later as to his qualifications in any way we can clear that up later.

Q. Mr. Bradley, between 1933 and 1937 what connection did you have with the Bradley Mining Company and its properties in the Yellow Pine area? A. Between what date and 1937?

Q. 1933, when you finished your studies at the University of California, and the year 1937?

A. During that period, first, I was during 1935 and 1936, working in the engineering staff at the Bunker Hill and made visitations to the Yellow Pine property, as I would come down through into Oregon to visit the quicksilver property. In 1937, late 1937, I took over the direction and management of that property. [34]

Q. Was the property then managed and operated from 1937 on, under your direct management?

A. Yes, not as a resident manager, but under my control.

Q. It was under your supervision?

A. Yes.

Q. Were you familiar with the ground itself?

A. Yes.

Q. Were you familiar with the engineering studies that were made in connection with it?

A. Yes.

The Court: Are you referring to the mining properties covered by this agreement?

Mr. Ray: Yes, I am, your Honor.

(Testimony of John Davis Bradley.)

The Court: Did you so understand, Mr. Bradley?

A. That he is referring to the Yellow Pine property.

The Court: And by the Yellow Pine property you mean all of the property covered by this contract?

A. Yes.

Q. Now, in 1937 there was no smelter there, was there? A. No.

Q. And the mining was being carried on under an agreement which had been dated in 1937, was it,—1930, I believe?

A. 1930 is correct. [35]

Q. What was being produced by the mining operation in 1937?

A. Gold antimony concentrates.

Q. Anything else at that time?

A. Not at that time.

Q. From your own examination of the property and a study of the engineering data accumulated at that time, did you expect that there would be yielded from the property values other than antimony and gold?

A. Yes, when the property was acquired in 1927 it was done mainly because of my father's interest in quicksilver and the adjoining property to this so-called Meadow Creek Group was known as the Cinnabar Group, and although during the 1930's the market was very weak, I should say because of the weakness of the market we did not pursue the development of the Cinnabar Group

(Testimony of John Davis Bradley.)

to the extent that we would have liked to have done, but we did recognize the possibilities there.

Q. At that time, was there any prospect of any other metal besides quicksilver, antimony and gold?

Mr. Casterlin: May I inquire now if the witness' testimony is with particular reference to the Hennessey and Meadow Creek Group?

Mr. Ray: Well, let's talk about the property covered by the 1930 agreement.

Mr. Casterlin: Then I think I will object to it as incompetent, irrelevant and immaterial for any [36] purpose as to the issues in this case, which are limited to the Hennessey and Meadow Creek Group.

The Court: Does this comprise more property than is covered by the 1930 contract?

Mr. Ray: I am limiting my question to the property covered by the 1930 agreement.

The Court: And does that include all or only a part of the property covered by Exhibit 7?

Mr. Ray: That includes all of the property covered by Exhibit 7.

Mr. Casterlin: And also other property.

The Court: And other property as well?

Mr. Casterlin: Yes.

The Court: Then your question, your inquiry now, is only as to the property covered by the 1930 agreement as included in Exhibit Number 7?

Mr. Ray: No, at this time it refers to all of the property covered by the 1930 agreement, and shortly I will come to the change from the 1930

(Testimony of John Davis Bradley.)

agreement to the '37 agreement and the '39 agreement, and it is in the '39 agreement that these controversial terms appear.

The Court: It is immaterial here what was expected to be produced from properties that may have been covered in the 1930 agreement that are [37] not involved in the agreement at the bar.

Mr. Ray: I think it is material and relevant, your Honor, for this reason,—when they changed the basis of their agreement from the terms of the 1930 agreement to the 1939 agreement, this provision of net revenue came into being, and at that time that was discussed and the reason for it was discussed between Mr. Bradley and the representatives of the other side,—we are looking for a reason,—under the customs of the smelting business everybody knows why the net smelter return provision is in the contract, but what is the use of this net revenue clause, what is it for?

The Court: Is that a part of the custom of the mining business, to have such a clause, is this net revenue provision a provision known to the mining industry or was it known only to these parties?

Mr. Ray: That is not a provision found customarily in the mining business.

The Court: But is it a term known to the mining industry as distinguished from known only to these parties?

Mr. Ray: That is a term that came in to meet certain purposes and situations as between these parties.

(Testimony of John Davis Bradley.)

The Court: That may have been, but my [38] question still is, was it a term known to the mining industry?

Mr. Ray: No.

The Court: As I understand it, net smelter returns is a terminology known to the mining industry.

Mr. Ray: That's right.

The Court: A phrase of definite connotation.

Mr. Ray: That's right.

The Court: And do you say that the term "mint returns" has the same standing?

Mr. Ray: That's right.

The Court: Does the term "net revenue" have the same connotation?

Mr. Ray: No, it doesn't.

The Court: Or the same standing in the mining industry?

Mr. Ray: It does not.

Mr. Casterlin: May I call attention to the fact that counsel, by this line of questioning, has moved up from the 1930 contract to the 1939 contract, and I want to make further objection to this testimony on the ground that the '39 contract, a portion of which appears on Page 85 of the Transcript, [39] provides as follows: "It is hereby specifically understood and agreed that this instrument of option, contract and agreement rescinds, nullifies, supersedes, and takes the place of all other contracts and agreements of every kind and character between the parties hereto and between the optionor and

(Testimony of John Davis Bradley.)

Fred W. Bradley and The Yellow Pine Mining Company, and that all such prior contracts and all negotiations between the parties hereto relative to the hereinbefore described properties, whether written or oral, of any kind or character, are merged herein, and that this agreement is to be construed without reference to any of said former agreements or negotiations." And in the light of the terms of that 1939 contract I am going to object until they can lay the foundation to show that it is proper to interpret the 1939 contract.

Mr. Ray: I would like to modify one statement which I made,—while the net mint returns and net smelter returns as stated are common, well recognized and universally used language in the mining industry, the mining industry uses other terms, various terms to fit varying situations, to take care of things that don't come either within the net mint or the net smelter returns. We have one of them here. Now, the exact language here doesn't follow any pattern that is recognized, by the same language, while the others are, the other terms are. [40]

The Court: It seems to me that certain customs and practices exist in the district with respect to disposal of products of a mine, and they would be relevant,—what are they, by what different methods were the products disposed of?

Mr. Ray: That is what I am getting at.

The Court: Here is a contract or agreement that the parties were formulating for a millennium

(Testimony of John Davis Bradley.)

or more, for 999 years, undoubtedly they drew from all of the knowledge and experience that they had in attempting to envision what might happen in 999 years in the mining industry. Now, there are various ways of disposing of products of a mine, what were the customs and practices in effect at the time, not what the parties meant by what they wrote in some previous document, but what were the practices and customs at the time this contract was formed, the contract in suit was formed, at that time. I will sustain the objection.

Q. Now, Mr. Bradley, prior to 1937 there was a cyanide plant at the Yellow Pine property, is that right?

A. Yes, but it only operated during 1932, which for a time produced bullion.

Q. Now, what was the custom and practice in the industry by which you got rid of gold bullion?

A. Sold it to the mint.

Mr. Casterlin: We object to that on the ground that it was prior to the 1941 contract, it is too remote, and on the further general ground that net mint returns, there is no argument about that.

The Court: As far as the circumstances surrounding the formation of the contract are concerned I don't suppose that there is any issue, is there?

Mr. Casterlin: No.

The Court: No, any cyanide process which produces gold bullion,—I suppose that has to be sold to the mint, doesn't it?

(Testimony of John Davis Bradley.)

Mr. Casterlin: It has to be sold to the mint.

The Court: Because of the requirement of the law, I think the law provides for that since, when, 1934. Since 1934 under the regulations and the law I suppose that all bullion has to be sold to the mint, making some exceptions, of course, but generally speaking, isn't that true?

Mr. Casterlin: That is correct.

The Court: The objection will be overruled.

Q. What was the practice of the industry with [42] respect to the disposition of antimony and gold concentrates?

The Court: At what time, Mr. Ray?

Q. At this time, prior to the 1939 contract.

A. They were sold to a smelter and we received net smelter returns.

Q. Now, what was the practice with respect to the sale of mercury, for instance?

A. Well, it is normally sold through a broker and you receive returns, usually from the final consumer.

Q. Was the settlement for mercury made as net smelter returns?

A. The theory of net smelter returns would cover, but technically it would be perhaps by a broader coverage.

Q. It never was sold at the smelter, was it?

A. Mercury, as a metal, it was sold to consumers.

Q. So that is a product not sold to smelters?

A. That's right.

(Testimony of John Davis Bradley.)

Q. Mr. Bradley, did you have something to do with the changing of the contract, from the 1930 contract to the 1939 contract? A. Yes.

Mr. Ray: I should like to offer the 1930 contract, it is marked as Exhibit Number 4 in the Oberbillig Deposition, the Oberbillig affidavit, which is in the record.

The Court: The Affidavit has been [43] filed, has it, and it has not been offered as an Exhibit?

Mr. Ray: It is marked as Exhibit Number 4.

The Court: Is there any objection to this offer?

Mr. Casterlin: We object to the offer of the entire Exhibit on the ground that it is incompetent, irrelevant and immaterial for the following reasons: It purports to be an agreement entered into on the 3rd day of October, 1930, between the United Mercury Mining Company and the Yellow Pine Company, and I object to it on the following grounds, that it has become merged in the 1939 contract, the '39 contract by its specific terms provides that its construction is not to be based upon anything which went before, and on the further ground that the relation between the parties in 1930 was that of lessor and lessee,—the relation between the parties in the contract of 1941 which is under dispute here now, is that of owner and payment of royalties. In other words, the Yellow Pine smelter, and the contract of 1930 was a lessee, and the contract of 1941, it is the owner. The contract of 1930 the United Mercury was the owner and lessor, and in the 1941 contract the United Mercury is the

(Testimony of John Davis Bradley.)

seller and receiving payment of the purchase price, the relation is not the same between the two. [44]

Mr. Ray: Do you object on the ground that Bradley is not a party to it?

Mr. Casterlin: No, Bradley is a party to the '30 agreement.

Mr. Ray: Let me call attention to this, the 1930 agreement, the parties are the United Mercury and the Yellow Pine Companies,—I will ask that question.

Q. Mr. Bradley, in the 1930 agreement, are the parties the United Mercury Company and the Yellow Pine Company? A. Yes.

Q. Who was the Yellow Pine?

A. The Yellow Pine Company in 1930 was owned 50% by my father and a quarter each by two other gentlemen.

Q. And the Bradley Mining Company succeeded to the interests of the Yellow Pine Company?

A. Yes, it took over its interests 100%.

The Court: The objection will be sustained on the ground that the 1930 agreement is irrelevant to any issues here. The Exhibit 4 may remain in the record if you so desire, as a record of excluded evidence. [See pages 253-339.]

Mr. Ray: I would like to include it there because we thought it was material and relevant because of the transition from that into this [45] net revenue and smelter returns as it first appeared in the '39 agreement.

The Court: My present view is that it is relevant

(Testimony of John Davis Bradley.)

and I will sustain the objection on that ground, and I will permit the agreement to remain in the record as I say as a record of excluded evidence, pursuant to the rules. We will take a five minute recess at this time.

March 19, 1957, 11:30 o'clock a.m.

Q. Mr. Bradley, I have handed you Exhibit Number 7, which is the contract of December 31, 1941, and I call your attention to the provision covering net smelter returns, net revenue and net mint returns, are you familiar with those provisions?

A. Yes.

Q. Were they in the previous contract?

A. Yes, they were in the 1939 contract.

Q. Is that the first contract they appeared in, the 1939 contract?

A. Yes, to the best of my memory.

Q. Who negotiated the 1941 contract, Exhibit Number 7, for the Bradley Mining Company?

A. I did.

Q. And who for the plaintiff? [46]

A. Mr. Oberbillig and Worthwine was the attorney.

Q. Mr. Oscar W. Worthwine?

A. Yes, Oscar W. Worthwine.

Q. Who negotiated the 1939 agreement for the Bradley Mining Company?

A. I negotiated it on behalf of the Bradley Mining Company.

Q. And who on behalf of the Plaintiff?

(Testimony of John Davis Bradley.)

A. Mr. Oberbillig and again that was with Mr. Worthwine as attorney.

Q. Did you confer with Mr. Worthwine and discuss the preparation of the 1939 agreement?

A. Yes.

Q. Before it was finally signed?

A. Yes, I did.

Q. Did you, at the time the 1939 agreement was prepared, discuss with Mr. Worthwine the provision which now is referred to as the net revenue provision?

A. Yes.

Mr. Ray: I offer in evidence Contract dated the 16th day of May, 1939, between the United Mercury Mines and the Bradley Mining Company, it has been identified as Defendant's Exhibit Number 5.

Mr. Casterlin: May I ask for what purpose it is introduced? [47]

Mr. Ray: I want to show, and I offer in evidence the conversations and understandings had with the parties with respect to the use and the purposes of the net revenue clause,—and how it got into that contract of 1939 and it is carried over with one slight modification in the 1941 agreement. I offer it upon this ground, your Honor, and we respectively submit that the Court cannot place himself in the situation in which the parties were when they made this agreement unless those vital circumstances are known to the Court.

Mr. Casterlin: We object to the admission of the Exhibit for that purpose, on the ground that it is incompetent, irrelevant and immaterial,—that the

(Testimony of John Davis Bradley.)

relation of the parties were not the same in 1939 as they were in 1941; that any preliminary discussion is presumed to have been merged into the final contract of 1941. In the contract of 1941 the parties, by their own agreement, have defined the meaning of the terms, and having so defined the meaning of the terms themselves it is immaterial what meaning any other person has, or what meaning one person has who was a party to the contract or what meaning another party has unless it is disclosed that there is some ambiguity, some uncertainty in the definition which the parties themselves have placed upon the contract.

The Court: Wouldn't it be a relevant [48] circumstance at the date of execution that there was in effect at the time the agreement was formulated this so-called 1939 contract?

Mr. Casterlin: That is a circumstance.

The Court: In the interpretation of the 1941 agreement?

Mr. Casterlin: Provided that there is some uncertainty, and this witness has not testified and there is no evidence here that there is any uncertainty in the definition of the terms of the 1941 contract, and the parties themselves have defined the meaning of the terms and they are bound by their own definition which they have placed on them.

The Court: The uncertainty may be in the application of something that is defined through a specific situation and the issues tendered here by the plaintiff is such an issue is it not?

(Testimony of John Davis Bradley.)

Mr. Casterlin: As to the application of clear, certain and unambiguous terms, the definition, to the operation of the Yellow Pine Smelter.

The Court: Yes, and that calls for an interpretation of the 1941 agreement, does it not, as applied to the Yellow Pine smelter operation?

Mr. Casterlin: To the interpretation of its application, not to the interpretation of the [49] meaning of any of the words.

The Court: Taking that position, assuming that situation, surrounding circumstances aid interpretation, that is, with that assumption it may aid in the interpretation and it may not, they are relevant to the issue as to the interpretation. Now the question immediately at hand is whether or not Exhibit 5 for identification is a material surrounding circumstance. It might aid in the interpretation of the agreement which follows. It seems to me that logically it might, however, it might not be of any substantial assistance, but isn't it relevant to the issue?

Mr. Casterlin: Not to the application to the Yellow Pine unless they can show that the parties were the same and the situation between the parties was the same, and that the same conditions existed there in 1939 as existed in 1941.

The Court: Weren't the parties the same?

Mr. Casterlin: Yes, they were the same.

The Court: So the question here is, is this a relevant circumstance surrounding the 1941 agreement? At the time it was formulated the 1939 one was in

(Testimony of John Davis Bradley.)

existence and was put out of existence by the 1941 [50] agreement.

Mr. Casterlin: Yes, there is no question about that.

The Court: It seems to me then that the objection goes to the weight of it and not as to the admissibility.

Mr. Casterlin: I have stated my objection.

The Court: Yes, and your observation assisted me in my ruling. I will overrule the objection and receive Exhibit Number 5 in evidence.

[See pages 339-371.]

Q. Mr. Bradley, who drafted, who wrote, Exhibit Number 5?

A. This being Exhibit Number 5.

Q. No, you have Exhibit Number 7, Exhibit Number 5 is the 1939 agreement.

A. Mr. Worthwine.

Q. In the course of your negotiations with Mr. Worthwine preliminary to the execution of Exhibit Number 5, did Mr. Worthwine submit to you a preliminary draft of the agreement? A. Yes.

Mr. Ray: I would like to have this document marked as Exhibit 5 A.

The Court: It may be so marked for identification. [51]

Mr. Casterlin: May I ask the witness a question in aid of objection?

The Court: You may.

Q. (By Mr. Casterlin): Mr. Bradley, are you

(Testimony of John Davis Bradley.)

familiar with what has been marked as Exhibit 5 A? A. I would like to see it.

(Document handed to witness.)

A. Yes, I am familiar with that.

Q. And is it a fact that it was the worksheet which was used prior to the final draft of the 1939 contract? A. Yes.

Q. And the 1939 contract then embodies the meeting of the minds after this was discussed?

A. I am not certain that the 1939 contract follows the exact wording of perhaps some of the changes made on here, but the principle was followed, yes.

Q. And the '39 contract became the final contract between the parties after these negotiations?

A. Yes, it became the final contract up to 1941.

Mr. Casterlin: Now, I will object——

The Court: It has not been offered yet, Mr. Casterlin.

Mr. Ray: I had not finished my preliminary questioning quite. [52]

Q. (By Mr. Ray): Mr. Bradley, was Mr. Worthwine a Boise lawyer? A. Yes.

Q. And long associated with the mining industry?

A. Yes, he was known quite prominently as a mining attorney in the State of Idaho.

Q. And he represented the Plaintiff in the negotiations which resulted in the finalization of Exhibit Number 5?

(Testimony of John Davis Bradley.)

A. Yes, and I think he was in the earlier one of 1937.

The Court: Is he living at this time?

A. Yes.

Q. Did he submit 5 A for your consideration?

A. Yes.

Mr. Ray: We offer Exhibit 5 A, of course, it has to be explained before its significance is apparent.

Mr. Casterlin: I now renew my objection to the offer.

The Court: I don't believe that you stated your objection, Mr. Casterlin, and—just a moment, the witness was volunteering something.

A. I simply want to say in answer to your question, your Honor, that Mr. Worthwine is still living and in active practice.

The Court: I had inquired whether [53] the attorney, Mr. Worthwine, was still living.

Mr. Casterlin: Yes, I see. Now, I will object to the admission of this Exhibit on the ground that it is incompetent, irrelevant and immaterial. By the terms of the Exhibit, the 1939 contract, it is specifically provided that it is to be interpreted without reference to prior negotiations, and on the further ground that it is a paper which was used by Mr. Worthwine in drafting the Exhibit and was not used by this witness, and what ever information he has now, it is indicated, would be peculiarly hearsay on his part.

The Court: The objection is sustained on the ground that Exhibit 5 A is irrelevant.

(Testimony of John Davis Bradley.)

Mr. Ray: May I examine the witness further with respect to some of the features of it, for the record?

The Court: You may make your record of excluded evidence, subject to the objection, pursuant to the Rules. Do you request that it be in your record as a record of excluded evidence?

Mr. Ray: I wanted to make a little further identification of it if I may.

Mr. Casterlin: I think the exhibit has been identified, and offered, and the offer has been denied, and any further questioning respecting the exhibit [54] is not proper.

The Court: You may make your objection and if Counsel desires then, of course, he may make the record.

Mr. Ray: Perhaps it would be better, your Honor, if I make an offer of proof in connection with this. May I do that?

The Court: I think the better practice is to make your record of excluded evidence, and then if the Court of Appeals decides that I am in error it is there for their consideration.

Q. Was Exhibit 5 A submitted to you by Mr. Worthwine as a basis for negotiation of the contract? A. Yes.

Q. Did it contain any reference to net revenue?

A. As I recall it——

Mr. Casterlin: I think, your Honor——

The Court: Do you object to any further questioning as to Exhibit 5 A?

(Testimony of John Davis Bradley.)

Mr. Casterlin: Yes, and on this question in particular, the Exhibit which has been rejected in the record now, of course, is the best evidence of what it contains.

The Court: The objection is sustained.

Mr. Ray: Then, may I offer to [55] make proof with respect to it, your Honor?

The Court: The document speaks for itself as to what it contains.

Mr. Ray: No, your Honor, it doesn't.

The Court: Then the witness may answer, you may make a record of it as excluded evidence.

Mr. Ray: So that it will not disturb the record, your Honor, may I make a statement off the record?

The Court: No.

Mr. Ray: There is information on this exhibit which I understand——

The Court: You may ask this witness any question you wish, and even though I sustained an objection to it he may answer it and the Answer will stand in the record as a record of excluded evidence under the Rule.

Q. (By Mr. Ray): Is there material on Exhibit 5 in your handwriting?

A. You mean Exhibit 5 A?

Q. 5 A. A. Yes.

Q. Was that placed on there in your handwriting after and during a discussion of the agreement with Mr. Worthwine? A. Yes, sir. [56]

(Testimony of John Davis Bradley.)

Q. And does the material that is in your handwriting constitute an amendment of the draft as submitted to you? A. Yes sir.

Q. And was the material which is on the draft and in your handwriting finally put in Exhibit 5?

A. Yes, the intent, I am not sure that each word follows, but certainly the meaning follows my suggestion there.

Q. Did you and Mr. Worthwine discuss the reasons why you proposed an amendment?

A. Yes sir.

Q. What discussion did you have with Mr. Worthwine with respect to the necessity of an amendment?

Mr. Casterlin: I am going to object to this as incompetent, irrelevant and immaterial for any purpose whatever.

The Court: I assumed that you objected to all of these questions respecting Exhibit 5 A.

Mr. Casterlin: Yes.

The Court: I assume this is offered not for the truth of what it says, or the fact, but to the fact that such words were said, is that correct?

Mr. Ray: I offer this to prove that the net revenue clause, which your Honor has to construe, came into this contract, the 1939 contract, as a result of a discussion between the representatives of the [57] two parties as to why it belonged in there, or why it didn't belong in there, and as to what it was intended to cover when it got in there, and that it

(Testimony of John Davis Bradley.)

was then brought over from the 1939 contract to the 1941 contract.

The Court: Has it been shown that Mr. Worthwine was an agent of the Plaintiff here at that time.

Mr. Ray: There is no doubt about it, as stated in Mr. Oberbillig's deposition, and counsel have never denied that he represented the plaintiff at that time, and he did his negotiating for him.

The Court: The objection is sustained on the ground that all of the objections to Exhibit 5 A are sustained. The witness may answer and his answer may remain in the record of excluded evidence pursuant to the rules. You may answer as to the conversation.

Mr. Casterlin: I might state, your Honor, that I was afraid he might be getting into matters that were beyond the scope of this Exhibit 5 A and that is the reason I made the additional objection.

The Court: Very well, you may answer, Mr. Witness.

A. Knowing that we had other values at the property, that would be perhaps, gold bullion, concentrates, and we had known of quicksilver and at one time we thought that there [58] might be a magnesium mineral that possibly could be recovered. We were hunting for a clause that would cover,—the net mint returns was in there, and we were hunting for a clause that would cover these other possibilities. Mr. Worthwine had one suggestion in there and I changed it with the objective of submitting it to him for his approval and Mr.

(Testimony of John Davis Bradley.)

Oberbillig's approval, a catchall clause that would cover all of these other things that we didn't know just what they might be. We knew of several, that the quicksilver didn't come under the net mint and technically it didn't come under net smelter, so that was the course of the conversation, and from that conversation the net revenue clause was picked up.

Q. Now, Mr. Bradley, is there some of your handwriting in Exhibit 5 A in connection with the net smelter provision? A. Yes, there is.

Q. And did you write something, as an amendment to that provision as proposed by Mr. Worthwine?

A. Yes, under the definition of net smelter returns I inserted the word normal between 'its' and 'smelting' so that it reads "It being understood that the smelter will deduct its normal smelting charges".

Q. Did you explain to Mr. Worthwine why that was desirable?

A. Yes, we discussed that point.

Q. What did you tell him? [59]

A. Well, I felt that on two counts,—one, that we had had difficulty with Mr. Oberbillig in the prior contract; that we wanted to catalog smelting charges as being customary, normal type of smelting charges. In the instance, number one, of our doing our own smelting, number two, as a protective device so that we could not overcharge Oberbillig. In my mind it was the customary way of cataloging smelting charges although the contracts that I am

(Testimony of John Davis Bradley.)

now familiar with do it with more language, they don't do it by defining it by the word 'normal'.

Q. That was a limitation then that you might assess in the event that you smelted your own ore?

A. Yes, and also a qualifying factor should we be shipping to some other smelter where Mr. Oberbillig might think the charges were too high, they were cataloged as normal, it was a protective, qualifying device.

Mr. Ray: In view of the witness' testimony, we take the liberty of re-offering Exhibit 5 A.

Mr. Casterlin: And we renew the same objection.

The Court: The objection is sustained. This concludes the testimony with respect to Exhibit 5 A, and the record will show that all of the testimony from the time it was first offered, which offer [60] was objected to and the objection sustained and offer rejected, all of your testimony subsequent to that portion of the record and up to this juncture constitutes a record of excluded evidence pursuant to the Rules.

Q. Now, Mr. Bradley, will you again refer to the provisions in Exhibit Number 7 for "net revenue". You will observe that it says "By net revenue as used herein is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties", does that clause "produced from said properties" have any accepted meaning in the min-

(Testimony of John Davis Bradley.)

ing industry according to the mining industry's customs and practices?

A. Yes, in my mind it does.

Mr. Casterlin: We object to this on the ground that it is incompetent, irrelevant and immaterial. The question of custom is not in issue in this case, and furthermore, it is not shown that there is any ambiguity in the terms or that there was any misunderstanding between the parties as to the meaning of the terms.

The Court: Is it proposed to be shown that the phrase "from said properties", that the term has a peculiar connotation in the mining industry different from its normal everyday meaning. I presume that it would mean that,—"from the property". If it means something else, you may show that. I take it that the parties may, if [61] a contract says black, the parties may show that in a particular industry black means white and that it was used in that sense.

Mr. Ray: It doesn't go that far, your Honor.

The Court: It is only when there is an issue as to whether or not the words mean something other than their normal signification.

Mr. Ray: Maybe I better ask a few preliminary questions.

The Court: It is after twelve now, and we will take the noon recess until two o'clock.

March 19, 1957, 2:00 o'clock p.m.

Mr. Ray: I would like to clear up a matter that may have caused some confusion.

(Testimony of John Davis Bradley.)

The Court: You may proceed, Mr. Ray.

Mr. Ray: This morning we started out to make proof of Mr. Bradley's qualifications to testify with respect to the custom and practice in the mining industry. I thought that our friends on the other side stipulated that Mr. Bradley was qualified to testify as to the mining custom and practice in general, as they relate to Idaho and the other western states. Now, if that is the [62] purport of Mr. Casterlin's stipulation I am content, but if there was a limitation to the state of California in his stipulation then I would have to pursue the matter farther.

Mr. Casterlin: I do not doubt the witness' qualification to testify as to the custom in the state of California, but I do question the materiality and the relevancy of the customs which existed in the state of California with respect to the issues in this case.

Mr. Ray: We understand, Mr. Casterlin, that you have reserved an objection to the materiality of all of this evidence. Do you agree that Mr. Bradley is qualified to testify with respect to the mining customs and practices as they relate to the State of Idaho,—smelting and mining?

Mr. Casterlin: Yes, we admit his qualifications to testify to those, reserving to ourselves the right to object on the ground of relevancy and materiality and so forth as to the time and the general location and things of that kind. We do not ques-

(Testimony of John Davis Bradley.)

tion his qualifications,—we question the relevancy of his testimony.

Mr. Ray: Then, your Honor, I would like to withdraw the last question and start a little farther back.

Q. Mr. Bradley, were you familiar with the custom of the [63] mining and smelting industry in the State of Idaho in 1939 and 1941? A. Yes.

Q. Did the industry, the mining industry, in that area recognize a distinction between mining and smelting?

A. Yes sir, I think in any area that is recognized.

Q. What was that?

A. In any area, any western area—or eastern—that is recognized.

Q. There is a distinction?

A. There is a distinction and has been a distinction.

Q. What is that distinction?

A. The distinction being that mining as such is merely the extraction of ores from the grounds and perhaps concentrations of them. Mining and concentration generally being considered in one general category. Whereas, smelting is the reduction of ores or concentrates to its metallic form.

Q. Aside from the custom and practice in the mining industry are there any laws or regulations which require a separation for accounting purposes of those two processes?

A. Yes sir, very definitely.

(Testimony of John Davis Bradley.)

Mr. Casterlin: Now, Mr. Bradley, before you go any further I think you have answered the question.

Q. What requirements are there?

Mr. Casterlin: We object to that as [64] incompetent, irrelevant and immaterial and it doesn't tend to prove or disprove any of the issues in this case.

The Court: You mean as to the law.

Mr. Ray: The requirements of the industry itself or the law.

The Court: Well, as far as the law is concerned the Court will take judicial notice of that.

Q. In the mining industry do you——

Mr. Casterlin: I have an objection, may I have a ruling?

The Court: I understand the question is being withdrawn.

Q. In accordance with the practice and custom of the industry do you keep the operations of the two separately?

A. For accounting purposes, yes.

Mr. Casterlin: Objected to as incompetent, irrelevant and immaterial, and not limited to the area in which the Hennessey the Meadow Creek groups are located.

The Court: Sustained in that form.

Q. Where is Bunker Hill?

A. Kellogg, Idaho.

Q. How far away is that from these mining properties?

(Testimony of John Davis Bradley.)

A. Approximately three hundred miles.

Q. What is the nature of the Bunker Hill operation?
A. Mining and smelting. [65]

Q. On a large or small scale?

A. Large scale.

Q. What products do they mine and smelt?

A. They mine lead, silver and zinc ores and smelt—

Q. Are those ores produced by the Bunker Hill Company?

A. By the Bunker Hill and by others and by properties 100% owned, 50% owned and on a lease and option basis.

Q. So that it is a custom smelter?

A. It is.

Q. In one part of its business and in the other part it smelts ore produced from its own properties?

A. Approximately 50% from its own properties and 50% from the outside, including Australia and South America.

Q. And it also treats ores arising from grounds which the company leases from others?

A. That is correct.

Q. Now, did they follow the customs and practices of the mining industry generally?

Mr. Casterlin: I want to object to that question on the ground that it calls for a conclusion on the part of the witness.

Mr. Ray: I thought you just stipulated that he was an expert on the subject.

(Testimony of John Davis Bradley.)

Mr. Casterlin: I did.

The Court: The objection is sustained. [66]

Q. Is there any difference in the practice and custom of the mining industry in one part of Idaho and the other?

A. No, in a general way, no.

Q. Now, is it the custom and practice in that area for separate records to be kept as to the production of the mine as distinguished from the production of the smelter? A. Yes.

Q. Was that so in 1939? A. Yes.

Q. Mr. Bradley, I think you stated this morning that you negotiated on behalf of the defendant, the contract of December 31, 1941?

A. Yes.

Q. That is Exhibit 7? A. Yes.

Q. On the other side Mr. Worthwine and Mr. Oberbillig represented the Plaintiff?

A. That is correct.

Q. When did these negotiations open, if you know?

A. Approximately in the spring of '41, but I am not positive as to the exact time.

Q. Did those negotiations continue during the months up until the contract was finally signed?

A. Yes.

Q. Did you discuss the matter both with Mr. Worthwine and [67] Mr. Oberbillig? A. Yes.

Q. Did you state to them your reasons for desiring a change? A. Yes.

Q. What were those reasons?

(Testimony of John Davis Bradley.)

Mr. Casterlin: Now, we object to this on the ground that it is incompetent, irrelevant and immaterial for any purpose in this action, and is an attempt to vary the plain, simple and unambiguous terms of a contract and the preliminary negotiations were all merged into the ultimate contract.

The Court: The objection is sustained on the latter ground, the last ground stated.

(Remarks by Mr. Breshears and the Court, reported and not transcribed.)

The Court: The objection will be sustained as stated and you may make your record of excluded evidence, if you desire, pursuant to Rule 43B.

Mr. Breshears: Thank you, your Honor, for your patience.

Q. Mr. Bradley, prior to the year 1941 was there any discussion with the Plaintiff in this case or any of its officers with respect to the possible construction of a smelter at or near the site of the property covered by the agreement? [68]

A. Yes, many times.

Q. When were those first discussions?

A. As far as I was concerned, probably in the late thirties, and so far as others representing my company were concerned, earlier than that.

Q. With whom were those discussions?

The Court: Is this all under your excluded evidence rule?—You don't care to make a record of the other matter?

Mr. Ray: I think maybe we should if we are permitted to do so.

(Testimony of John Davis Bradley.)

The Court: Yes, you may, absolutely.

Mr. Casterlin: Then I understand these questions are under the excluded evidence rule as announced by the Court.

The Court: Yes, there was a question pending to which the Court sustained an objection, do you wish it read?

Mr. Ray: Yes, please.

(Question read by reporter as follows:

“What were those reasons?”)

Mr. Casterlin: That was the question to which there was an objection directed.

The Court: And sustained, and the evidence excluded. [69]

Mr. Casterlin: I would like to be advised by counsel when he terminates his examination on this point.

The Court: Do you understand the question?

A. No, I am a bit lost, what were those reasons, —I don't remember just before that.

Q. You stated that negotiations for the 1941 contract began sometime early in the year and that you discussed the matter with the representatives of the plaintiff, and I asked you then if you stated the reasons why you wanted the contract changed, and you said “Yes,” now, what were those reasons?

A. The reasons were that the '39 contract, in our minds, was going to become burdensome owing to the royalty, the graduated royalty schedule contained in it.

Q. The royalties were too high?

(Testimony of John Davis Bradley.)

A. The royalties were higher than we thought we could economically bear. In other words, ore that would be ore under a certain royalty would not be at the higher rate of royalty.

Q. Would that then, in effect, place a limitation on the mine? A. Yes, sir, oh yes.

Q. Now, coming to another subject, Mr. Bradley—

The Court: —Was this told to the Plaintiffs?

A. Yes, as the reason, our reason for wishing it.

The Court: I will reverse the ruling on that, I think that should stand,—that answer, as the reason why the contract, why the 1939 contract was terminated and the new contract was negotiated. It being a motive or purpose expressed to the other party, that, in my opinion, would be admissible.

Q. Now, Mr. Bradley—

The Court: —So that the last answer will stay in the record,—I want the record to be perfectly clear on that.

Q. You state that in the late thirties you began discussion with the other side with respect to the possible construction of a smelter at the site, is that correct?

A. I didn't begin serious discussion with them pertaining to the point, no. I mentioned to them that we were carrying on research toward the best method of local reduction and would report periodically as to our progress.

Q. Did those studies continue?

A. Yes, they continued.

(Testimony of John Davis Bradley.)

Q. Over what period of time?

A. Starting in the early thirties every bit of work was a step ahead in the next phase and the latest work was what was being undertaken, was being done on our behalf by the research laboratory up at Kellogg, by the Bunker Hill [71] Company, and that was done to the best of my recollection in the late thirties and up until about war time.

Q. Until about the war time?

A. About 1941, and then it was picked up again around about 1944 or '45.

The Court: So that the record will be absolutely clear here, gentlemen, I mean, it is clear to me but I don't know whether the record is clear for a rehearing, and I don't know whether it is clear to you. I reversed that ruling so that there is no record of any evidence excluded and so that none has been excluded since the morning session.

Q. Was that during the years from time to time discussed with either Mr. Worthwine or Mr. Oberbillig? A. Yes.

Mr. Ray: Might I remind your Honor that Mr. Worthwine was a beneficiary under the 1941 contract.

Q. After the 1939 contract was signed, and before the 1941 contract was signed, was there any discovery on this property covered by this litigation, of any product which could be mined and which could be mined and which would not or could not be sold to a smelter? A. Yes, sir.

(Testimony of John Davis Bradley.)

Q. What product was discovered on the property? [72] A. Tungsten.

Q. When did you discover the existence of tungsten in the property?

A. We were made aware of it by a telegram from the United States Geological Survey in early February of '41. I should add to that, Mr. Ray, that we also were conscious of mercury being on the Cinnabar deposit and at any time might be discovered on the main Meadow Creek and Hennessey property.

Q. In connection with that mercury, I don't know whether I asked you before, but so that I will be sure and have it in the record,—does mercury occur sometime in the earth in a metallic form or free mercury? A. Yes, it does.

Q. And if you get free mercury in the earth, after you extract it, what do you do with it,—I will put it this way, do you send it to a smelter?

A. No, after you mine your cinnabar which is the most common occurrence of mercury, you roast it and condense the fumes and recover the finished product.

The Court: Where is that done, Mr. Bradley?

A. That is normally done right at the property, regardless of size, it can be a very small deposit, in which case they merely retort it.

The Court: Why is it done on the [73] property, is there any particular reason?

A. Normally you wouldn't want to haul that

(Testimony of John Davis Bradley.)

low grade material,—the low grade bulky material, and you concentrate it by this process.

Mr. Casterlin: I wonder if the witness would speak a little louder, I don't hear him.

A. You wouldn't want to haul the low grade bulky material owing to the economics, and it is so cheap to reduce it right on the spot.

The Court: Then, as I understand it, with respect to the so-called cinnabar, mercury bearing ore, it was, at the time the contract was formed, the custom and practice in the mining industry to roast the ore at the sight of the mine and get the mercury out of it there and sell the mercury, the finished product, because it was not economical *the* transport the ore itself some distance.

A. The answer is yes.

Q. Mr. Bradley, according to the custom and practice in mining country, is that treatment which relates peculiarly to mercury regarded as mining or smelting?

A. It is regarded as mining.

Q. When did you start, if you did start, mining tungsten?

A. In the late summer of '41 and started up the concentrator, as I recall it, in August and made our first shipment late [74] that month,—in August of 1941.

The Court: Will you tell us at this point, you have been discussing the practice of the mining industry in Idaho at this time, in 1941, what was

(Testimony of John Davis Bradley.)

the practice with respect to the production of that tungsten, can you tell us?

A. Yes, tungsten occurred as about one and a half per cent grade of the radical W03, tungstic oxide, the mineral being scheelite, calcium tungstate, CaW04.

The Court: And that was a deposit you found on this property? A. Yes.

The Court: And what was the custom and practice at that time with respect to handling and processing this scheelite?

A. In order to market that ore it had to be concentrated to at least sixty per cent.

The Court: And how was that done?

A. That was done by a combination of flotation and gravity concentration method.

The Court: And where was that done?

A. That was done at the property.

Q. And why was it done at the property, rather than at some other place? [75]

A. Again because of economics and the freight being such a factor, it was so much cheaper to do it on the spot rather than haul it eighty miles and bear a freight cost against the low grade ore.

The Court: Eighty miles being the distance from where to where?

A. From this property to the railroad at Cascade, Idaho.

The Court: You have described what you consider good business mining practice at this point at that time, and my question deals with what was

(Testimony of John Davis Bradley.)

the custom and practice in the industry with respect to that type of ore in that community at that time, not what you did in this case but what was the general practice and custom in handling the ore?

A. It was exactly the same.

The Court: As you have described?

A. Yes.

The Court: And for the same reason?

A. That is correct.

Q. Now, Mr. Bradley, you have described to His Honor how that material was handled, will you state whether or not, in accordance with the custom and practice, was that regarded as **mining or** smelting? A. Mining.

Q. Is it a fact or isn't it that what you did to that was [76] milling, in the sense that milling is a term understood by the mining industry?

A. I call it concentration.

Q. Is it milling? A. Yes.

The Court: Do you call mercury ores, cinnabar ores, do you call that quicksilver?

A. Yes, they are referred to as quicksilver.

Q. Were any of those antimony concentrates or tungsten concentrates which you mined in the fall and summer of 1941, disposed of by you?

A. You say were the concentrates, the **tungsten** concentrates, disposed of by us?

Q. Did you dispose of the tungsten concentrates in 1941?

A. Yes, we commenced shipment in either late August or early September of 1941.

(Testimony of John Davis Bradley.)

Q. Were they sent to smelters? A. No.

Q. Or mints? A. No.

The Court: Now, what was the custom and practice of the mining industry in that community at that time in disposing of that tungsten?

A. Your market was entirely in the eastern United States, and with a very few limited consumers. In our particular case—— [77]

The Court: ——Was it to sell them somewhere else? A. Yes.

The Court: Ship them somewhere and sell them, was that it?

A. Yes, practically every consumer was east of Chicago.

The Court: Then, as I understand it, the custom and practice at that time, in 1941, in that community, was to mine this tungsten ore and put it through this flotation process which you described, and concentrate its value, and then ship the concentrate somewhere east of Chicago to a market.

A. That is correct.

Q. And was that practice which you followed in accordance with the general practice in the mining industry? A. Yes.

Mr. Casterlin: I am going to object to that because it is in conflict with the answer he has just given, it is immaterial if it has relation to any area outside of the area of these particular claims.

The Court: As I understand it, it was a repetition of the question that I just asked.

(Testimony of John Davis Bradley.)

Mr. Casterlin: Then if it is I have no objection.

Mr. Ray: I just wanted to make [78] sure of it.

The Court: Are you referring to this locality in northern Idaho?

Mr. Ray: That is the way they did it in Northern Idaho, but I wanted to know whether that practice in Northern Idaho was in accordance with the general practice in the industry, I thought you asked that question but I wanted to be clear on it, I wasn't sure.

The Court: I didn't ask with respect to if it was the custom anywhere else, if the question refers to the custom in any other community then, of course, that might be objectionable.

Mr. Casterlin: That is the question as I understood it and to which I made my objection, as being immaterial.

The Court: Suppose the custom was different in Nevada or down in California, would it be material here? What we are interested in was the custom here. Of course, the practice,—well, it might be material if it was shown that it was a widespread custom.

Mr. Casterlin: But custom is not in issue here.

The Court: We are receiving evidence of custom and practice as one of the surrounding [79] circumstances. The question is, is it the custom and practice in the entire mining industry, or is it the custom and practice merely in this community at this particular time?

(Testimony of John Davis Bradley.)

Mr. Ray: I want to make one point clear here if I may. Some people think that Stibnite, the community mentioned here, is in Northern Idaho, and some think it is in Central Idaho, but I take it that your Honor doesn't make any point by the use of the words "North Idaho."

The Court: Perhaps I should not have said north. I mean where this property is. I am talking about the time this contract was negotiated and formed, and I am talking about that particular territory. If you want to show that this custom not only prevails in that community but was the custom throughout the mining industry, I will permit you to do so. You may also show, if you so desire, that it was not only the custom at that time but was the custom from time immemorial, if that happened, I don't know. The reason I would allow it is that it seems to me that it would be material in interpreting a contract that the parties intended to run for nearly a thousand years.

Q. Can you state how wide that custom and practice was at that time? [80]

A. In the case of tungsten?

Q. Yes.

A. Tungsten had to be concentrated in order to be shipped to eastern markets unless it was sufficiently high grade to be shipped as ore.

Q. And was the practice that you followed up there in accord with the general practice throughout the mining area?

A. Yes, with the exception that we had to float

(Testimony of John Davis Bradley.)

our sulfides out first, we had a more complicated situation, but, in general, we followed the normal practice.

Q. Did you ship substantial quantities of that during the fall of 1941? A. Yes.

Q. Did that become an important part of your mining operations in the years beginning with the year 1942?

A. It became the most important part in the history of the mine from beginning to end.

Q. For how long a time did you continue to mine tungsten?

A. Through '44 and into part of '45 as I recall.

Q. State whether you continued all through those years to treat the material and send it to purchasers other than smelters? A. Yes.

Q. Did you at any time after December 31, 1941, subject any of your tungsten concentrates to any process which [81] was outside the realm of mining before you disposed of it? A. Yes.

Q. Where was that done? A. In Boise.

Q. In this city? A. In Boise, Idaho.

Q. What did you do with the tungsten ore at the mine before the product was shipped to Boise?

A. Concentrated them.

Mr. Casterlin: May I ask what year that was?

Q. When did you begin that?

A. I believe that was in late '43, it may have been early '44.

Mr. Casterlin: We object to this on the ground

(Testimony of John Davis Bradley.)

that it does not aid in anyway in determining the contract prior to the time it was drawn.

The Court: Is the purpose of this to show an interpretation placed by the parties, upon the contract, subsequent to its execution? It would be relevant to that, would it not?

Mr. Casterlin: Yes, but I want to find out the purpose.

The Court: Before you leave the question of the custom and the practice existing at the [82] time the contract was formed, was there in the history of tungsten mining or in the mining of tungsten ore, did you ever know of any custom or practice to send the ore to a smelter? A. No.

The Court: In the history of mining quicksilver ore, did you ever hear of any custom or practice of sending any of that ore to a smelter?

A. Yes.

The Court: Your answer is yes?

A. I don't think it applies here, but in case of a quicksilver antimony ore from Mexico, it did go to a smelter, but it is an odd case.

The Court: Is that an isolated instance?

A. An isolated instance, yes.

The Court: In all of your knowledge of the mining history, did you ever know of any other instance of quicksilver ore being sent to a smelter?

A. Not a smelter as we know it.

The Court: What do you mean by "smelter as we know it?"

A. What we are talking about in this instance

(Testimony of John Davis Bradley.)

here, as a smelter, is one that will reduce metals such as lead, [83] copper or zinc to their metallic form,—lead, copper, zinc or antimony. In the case of mercury it does have a heat treatment.

The Court: That is called a roasting treatment?

A. Roasting, but even roasting is a form of smelting, but nevertheless the Internal Revenue didn't catalog it as a part of the smelting process because it's so simple.

The Court: Did the term "smelting," in the mining industry, at this time did it have, and has it always had, some special signification?

A. Yes, you don't speak of quicksilver as being smelted.

The Court: What is the content of the process referred to as smelting?

A. In simple form it is roasting away the sulphur, reducing then the oxidized mineral to metal and refining the impurities away.

The Court: Are there separate steps,—three steps?

A. Roasting, reduction and refining.

The Court: Three essential steps of smelting?

A. Yes.

The Court: Has that always been so? [84]

A. Yes. May I add, your Honor, in the case of tungsten, so that we are absolutely clear,—tungsten, being an oxide, goes through a heat process to be reduced to a metal, but that isn't called,—we don't think of it as smelting.

(Testimony of John Davis Bradley.)

The Court: Where does that take place customarily?

A. Customarily on the eastern seaboard.

The Court: The purchaser of the concentrates does that? A. Yes, that's correct.

Q. (By Mr. Ray): You were just about to tell us about this Boise plant, what did you call that?

A. We called it the Boise purification plant.

Q. To what treatment were the concentrates mined subjected to in the Boise purification plant?

A. Phosphorus, arsenic, antimony and sulphur were all removed.

Q. By heat?

A. By heat and leaching. We remove the phosphorus by leaching with hydrochloric acid, remove the antimony by leaching with caustic soda and we roasted off the remaining antimony, some arsenic and some sulphur, by heat.

Q. Was that a part of that treatment outside of what the mining [85] industry recognizes as mining?

A. Yes, I would call the roasting step there beyond—at a higher temperature than we would use in mercury and therefore over into the smelting phase. Furthermore, the change in the nature of the material by the removal of lime and the removal of these other impurities goes beyond a normal ore dressing.

Q. Now, was the product which resulted from the Boise treatment sold to customers in the east?

A. Yes.

(Testimony of John Davis Bradley.)

Q. Did you compute royalties on the proceeds of those sales? A. Yes.

Q. Did you periodically report to the Plaintiff the proceeds and show how the royalties were computed? A. Yes, monthly.

Q. And did you deduct from the amount received for those products the cost of the Boise treatment? A. Yes.

Mr. Casterlin: May I suggest here to counsel, if you have a sheet illustrative of the report then I won't have to object that the report is the best evidence.

Mr. Ray: I was going to offer some of those by another witness, but I don't object to producing one at this point. [86]

The Court: Introduced just as an exemplar——

Mr. Casterlin: Oh, yes.

The Court: This will be Exhibit 29 in this case.

[See page 417.]

Q. Will you examine the document which has been marked as Exhibit 29, Mr. Bradley, and explain to His Honor what that is

A. This is evidence of a shipment from our Boise purification plant to Sylvania Electric Products Company. It shows the gross sales per the attached invoice which is the actual invoice to Sylvania less the operating costs——

The Court: ——The gross sales of what?

A. Shipment of tungsten which had been processed at the Boise purification plant, less the op-

(Testimony of John Davis Bradley.)

erating costs at the Boise purification plant, including depreciation.

Q. May I ask you one or two questions for the purpose of clarification. Does this—withdraw that—this indicates that it is an invoice, this first page, is that right?

A. I don't know which is your first page, but the big sheet is mine.

Q. The long sheet? [87]

A. The long sheet is the invoice, yes.

Q. And it is identified as B-13-B? A. Yes.

Q. This is an invoice covering a lot number?

A. Correct.

Q. It indicates a sale of products to the Sylvania Electric Products Company of Towanda, Pennsylvania? A. Yes.

Q. And the product covered by this invoice was material shipped out of the Boise purification plant, is that right? A. Yes.

Q. There is a figure near the bottom of the page,—\$34,228.93, is that correct?

A. That is correct.

Q. Is that the amount paid to the Bradley Mining Company by the Sylvania Electric Products Company, Incorporated? A. Yes.

Q. What is the short sheet?

A. The short sheet was our evidence to the United Mercury Mines Company of this shipment, of the receipt and less our charges for processing that material.

Q. Now, was the invoice, in this particular case,

(Testimony of John Davis Bradley.)

B-13-B, and the report showing the receipts from Sylvania less deductions sent to the Plaintiff? [88]

A. Yes.

Mr. Ray: We offer Exhibit 29 in evidence.

The Court: In other words, copy of this invoice plus what you call the report, those two together was the accounting,—constitute the accounting made to the Plaintiff, of this particular transaction?

A. Yes, sir.

The Court: And was a like accounting made over a period of years for like shipments?

A. Yes, sir, be it a smelter or be it any other consumer, it would be the net smelter return or the invoice.

The Court: Is there any objection to this offer?

Mr. Ray: I might say, your Honor, these are copies, but the other side, presumably, has the originals.

Mr. Casterlin: May I ask a question in aid of an objection?

The Court: You may.

Q. (By Mr. Casterlin): Mr. Bradley, you testified to the Exhibit 29 and you called attention on the short sheet to an item less operating cost applicable, including depreciation. You mailed these to the United, did you? [89]

A. Yes.

Q. You mailed them a check? A. Yes.

Q. Was there ever any objection to that item?

A. No, none.

Q. You know of no objection?

(Testimony of John Davis Bradley.)

A. No, I don't.

Mr. Casterlin: No objection.

The Court: Exhibit 29 may be received. The amount shown, for Exhibit 29, from Sylvania. From that you deducted the actual cost of this operation at the purification plant, is that it?

A. Plus the depreciation,—including the depreciation, which is a part of the cost.

The Court: A part of the cost? A. Yes.

The Court: In other words, you did it without a profit? A. That's right.

The Court: At the estimated cost for the processing? A. Yes.

Q. (By Mr. Ray): Mr. Bradley, you testified that other reports and invoices similar to Exhibit 29 were sent monthly during all the time you operated the Boise purification plant. [90] As near as your recollection serves, can you tell us when that began and how long it persisted?

A. I believe it began in 1943 and persisted into '45, but I would have to double check to be absolutely positive about that,—1943 into 1945.

Q. Now did anybody representing the Plaintiff, United Mercury, ever complain or object to that method of settlement? A. No.

Q. Did Mr. Worthwine ever complain or object about that settlement? A. No.

Q. When you began—

The Court: Before you leave that,—over what period of time did this manner of handling tungsten through the Boise purification plant take place?

(Testimony of John Davis Bradley.)

A. I think it was close to two and a half years.

The Court: And over that period of time how often did you make accounting to the Plaintiff, similar to Exhibit 29?

A. We made monthly accounting and normally there would have been shipments out of there every month. There should have been an accounting almost every month,—an accounting of receipts. [91]

The Court: During the entire period?

A. Yes—I wouldn't say every month, but every month there was a shipment there would have been an accounting.

Q. Mr. Bradley, when you began production of tungsten concentrates in an important way, did you discontinue the production of other ores and concentrates?

A. No, on the contrary. Once we got into the tungsten the other minerals increased, like antimony, so that we had a greater production of antimony.

Q. Was that because the antimony resulted as a by-product of the tungsten?

A. Yes, the antimony didn't hold the value that the tungsten did.

Q. How did you dispose of the other products?

A. We shipped them wherever and whenever we could, and finally made fairly steady arrangements with the Harshaw Chemical Company of El Segundo, California, for the shipment of antimony concentrates.

(Testimony of John Davis Bradley.)

Q. Did they operate a smelter there for the treatment of antimony concentrates?

A. They happened to have an inadequate plant for the receipt of our concentrates and spurred by the Government they built a completely new plant there under D.P.C. for the receipt of these concentrates. [92]

Q. Was that a smelter?

A. That was a smelter.

Q. Did you from time to time following January 1, 1942, ship antimony concentrates to Harshaw Company at El Segundo?

A. To Harshaw Chemical and numerous others about the country, including the Laredo Smelter, at Laredo, Texas, the Chemical and Pigment at Baltimore, to the Federated Division at A. S. and R. at Whiting, Indiana.

The Court: What is A. S. and R.?

A. American Smelting and Refining.

The Court: And what is D.P.C.?

A. Defense Plant Cooperation.

Q. So that you had more than one outlet during those years for this antimony concentrate?

A. Yes, during the wartime there was a demand for antimony in addition to tungsten.

Q. And are we correct in understanding then, Mr. Bradley, that these antimony concentrates were shipped to smelters?

A. Yes, with the exception, Mr. Ray, of one or two instances where it was used as a precipitant in a process,—that was a wet process. I just don't

(Testimony of John Davis Bradley.)

want to say that it all went to smelters because it didn't. There were one or two instances where it didn't. [93]

Q. Some of the antimony concentrates were disposed of to purchasers other than smelters?

A. Yes.

Q. Did you continue to produce gold concentrates? A. Yes.

Q. When you speak of gold concentrates is that a concentrate which is particularly valuable for its gold content?

A. Yes, gold being the most valuable.

Q. Was there, in the gold concentrates, some antimony? A. Yes.

Q. You have spoken of antimony concentrates, are we to assume that when you refer to antimony concentrates you are referring to a concentrate or product which is particularly valuable in antimony?

A. That is correct.

Q. Did the antimony concentrates contain some gold? A. Yes, sir.

Q. Where did you dispose of your gold concentrates?

A. Mainly to the American Smelting and Refining Company's plants at Garfield near Salt Lake City and at Tacoma, Washington.

Q. How were you paid for those products?

A. On the basis of net smelter returns.

Q. What does the term "net smelter returns,"—what is it understood to mean in the mining industry? [94]

(Testimony of John Davis Bradley.)

Mr. Casterlin: I think it is stipulated in the Pre-Trial Order about the net smelter returns.

The Court: Is it covered by the Pre-Trial Conference Order?

Mr. Casterlin: Yes, your Honor.

Mr. Ray: We would like to have the Pre-Trial Order considered as a part of the record by the Court, and we offer it in evidence as such.

The Court: Is there any objection to that?

Mr. Casterlin: No objection.

The Court: It may be admitted and received as Exhibit Number 30. Now, Gentlemen, if this is covered by the agreement we don't need to take the time here on it.

[See page 419.]

Mr. Casterlin: It is covered by the definition which the parties accepted for themselves and put into the contract of 1941.

The Court: Where is it referred to in the Pre-Trial Conference Order? I understood you to say that it was in the Pre-Trial Conference Order, that's what we are interested in right now. The term is used in Paragraph K at the bottom of Page 5 of the Pre-Trial Order. Perhaps we can cover it with a question or two rather than look for it. Mr. Bradley, does the term, or did the term, [95] "net smelter returns" have any special signification in the mining industry at the time the 1941 contract was negotiated and formed?

A. Yes, your Honor, it——

Mr. Casterlin: ——May I interpose the objection

(Testimony of John Davis Bradley.)

that the term "net smelter return" has been defined by the parties themselves in plain, simple and clear language as found in the Exhibit which has been admitted as the contract of December 31, 1941, the language which appears on Page 17.

The Court: Will you read that to me?

Mr. Casterlin: "By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted."

The Court: The objection is sustained.

Q. Mr. Bradley, when concentrates are sold to a smelter does title pass to the purchasing smelter?

Mr. Casterlin: I think that is answered by the answer to our interrogatories. [96]

A. —May I ask whether you mean as a general practice?

The Court: You don't need to pursue that right now, we will take our afternoon recess at this time.

March 19, 1957, 3:25 O'Clock P.M.

Q. Mr. Bradley, I think that you stated that you are familiar with the custom and practice under which concentrates are sold to custom smelters, is that right? A. Yes.

Q. Was Harshaw a custom smelter according to your understanding? A. Yes.

Q. And Bunker Hill, your own smelter, is a cus-

(Testimony of John Davis Bradley.)

tom smelter? A. Yes.

Q. Were National Lead and Laredo custom smelters? A. Yes.

Q. Is it customary in the industry when concentrates are sold to a custom smelter, to provide for the deduction of normal smelting charges?

Mr. Casterlin: I think that is covered by stipulation and deposition.

Mr. Ray: I am referring to the word "normal."

Mr. Casterlin: I think we have defined [97] the word "normal" when we have agreed on the net smelter returns, and we have in here an exemplar.

The Court: Isn't it the gross less the reasonable and necessary cost of smelting?

Mr. Casterlin: Yes, as I say, we have an exemplar here and we have submitted reports, they are Exhibit 3, which are attached to the Complaint.

Mr. Ray: My point was that when you deal with an outside smelter, or when you sell to an outside smelter, you don't have anything to do with what the man you are dealing with is going to deduct, he either buys your product or he doesn't, but you have the word "normal" or its equivalent in the mining industry when the ore is treated by the smelter, and only then. Normal means nothing in connection with the sale of concentrates to a custom smelter, it has a meaning in the industry only when the smelting company is also mining.

The Court: Wouldn't it have its ordinary signification, what is usual, a normal charge is what is usually charged.

(Testimony of John Davis Bradley.)

Mr. Ray: There is no such thing as usual in connection with the sale of concentrates to a custom smelter. There may be treatment charges.

The Court: Isn't there such a [98] thing as something usual in connection with the charge that the smelter makes?

Mr. Ray: That is what I want to ask this witness about.

The Court: I understand there is no issue between the parties on that.

Mr. Casterlin: There is no issue and I will make the further objection on the ground that the parties have defined what they mean by "net smelter returns."

The Court: This deals only with "normal" as it is in the definition.

Mr. Ray: It says, under net smelter returns, that the smelter will deduct its normal smelting charges, they shall be allowed to deduct the normal smelting charges.

The Court: To me that means that the smelter may deduct what is ordinarily charged for those services.

A. When we sell to someone outside we have no control over what he deducts, we do if we smelt it. Now, in the Boise purification plant if we undertook to charge excessively, he could complain, he could say, no, you are charging too much.

The Court: That would be abnormal, wouldn't it? [99]

Mr. Casterlin: There is another situation here,

(Testimony of John Davis Bradley.)

too, we have stipulated and agreed that so far as the reports are made on these smelter returns, there is no objection to it.

The Court: As I understand it, you offer to stipulate that the word "normal,"—first, I understand that the word "normal" is used in the definition of "net smelter returns" in the contract?

Mr. Casterlin: Yes.

The Court: And are you agreed as to what 'normal' means as there employed?

Mr. Casterlin: We are to this extent, that the normal charges are those which are included in the exemplars which we have admitted in evidence as being samples of smelter returns.

The Court: Aren't they the charges that smelters customarily make for that service?

Mr. Casterlin: Yes.

The Court: And wouldn't that be normal, it seems it would be to me unless it is used in some extraordinary sense I would say that the ordinary and usual signification of the word would be the usual, customary charge.

Mr. Ray: But that is not a term used customarily in the mining industry in connection with [100] the sale of concentrates to outside smelters.

The Court: I don't follow you, Mr. Ray, I am sorry.

Mr. Ray: I don't like to do the testifying.

The Court: No, that's right, but if there is no issue between you as to what the word "normal" means, why need we go into it?

(Testimony of John Davis Bradley.)

Mr. Ray: Your Honor, if I want to sell concentrates to the Harshaw Company from this property I don't say to them "I will sell these concentrates and you shall deduct normal smelting charges," that would be entirely contrary to custom and practice.

The Court: What do you say?

Mr. Ray: We say we will sell you these concentrates, what will you pay for them, and they say so much, here is a schedule.

The Court: Does that include the deductions ordinarily and usually made, normal deductions?

Mr. Ray: That might be entirely different than what somebody else would give for them.

The Court: Are you suggesting, Mr. Ray, that it is the practice and custom of the industry not to have any smelting charge, as such?

Mr. Ray: No, but I say this, you [101] have different situations. When I sell my concentrates to outside smelters I don't provide that he shall deduct normal or abnormal smelting charges or anything else.

The Court: But this contract provides "net smelter returns," contemplating that, doesn't it?

Mr. Ray: It provides that when I get to the smelter I will give him five per cent, smelting returns.

The Court: Is that the definition? The definition is "gross, after deducting the normal smelting charges plus transportation."

Mr. Ray: That's what I get from the smelter,

(Testimony of John Davis Bradley.)

the smelter deducts those charges.

The Court: Yes.

Mr. Ray: Now, if I smelt my own concentrates that question doesn't arise unless there is something, unless—it is from leased ground. And then, in order that I don't charge an indefensible treatment charge then I use the word "normal," and then only, or its equivalent.

The Court: The "normal" means just that, normal and reasonable, I suppose.

Mr. Ray: I think so.

The Court: It has been stipulated [102] here that whatever was deducted was a reasonable charge. Whatever has been deducted by the defendant for services of the Yellow Pine Smelter is a reasonable charge, isn't that stipulated by the Plaintiff?

Mr. Casterlin: That is the way I understand it.

Mr. Ray: It is stipulated that if we are entitled to any credit then the charge we have made is reasonable.

The Court: What's the difference?

Mr. Ray: Because this phrase "normal" indicates that this net smelting returns provision, also by the use and introduction of that word normal, it applies to our smelter, that is the factor that is in the contract that doesn't apply.

The Court: What do you propose to show by the witness?

Mr. Ray: I want to show that if they had contemplated that we would treat these concentrates

(Testimony of John Davis Bradley.)

in our own smelter and make smelting deductions for it, that word "normal" never would have been in the contract.

The Court: This witness won't be permitted to say that.

Mr. Ray: I wanted to point out, if I may, that this is the only type of contract in the [103] industry where the word "normal" is used.

The Court: Is there a pending question?

A. I was asked whether the word "normal" was in common useage in cases, I think the intent being non-lease ground.

Q. On sale to custom or outside smelters?

The Court: Suppose you rephrase the question, Mr. Ray.

Q. Is the word "normal" customarily used in connection with the sale of concentrates to outside smelters? A. No.

Mr. Casterlin: That can be answered yes or no.

A. The answer is no.

The Court: I think possibly there was an objection to that question that I have not formally ruled on.

Mr. Casterlin: If the other question is withdrawn, I will not press the objection.

The Court: Very well.

Mr. Casterlin: I do not press any objection to this last question.

Q. You have given us some testimony with respect to study and discussions about the construction of a smelter at or near [104] the property

(Testimony of John Davis Bradley.)

which is described in this Contract, Exhibit Number 7. Did that discussion between you and the other side ever involve the possibility that some outsider would build a smelter there? A. Never.

Q. According to your discussion, if the smelter was to be built at or near the site, who was to build it?

Mr. Casterlin: I am going to object to that as incompetent, irrelevant and immaterial, and not tending to prove or disprove any issue in this action, and not pertaining to the clarification of any of the terms of the contract or its application to the Yellow Pine.

The Court: The objection is sustained to the question in that form on that ground. Are you attempting to elicit from this witness that there was, during the negotiations, a discussion between the Plaintiff and the Defendant about the possibility of the defendant or someone else building a smelter at the site, is that what you propose to show?

Mr. Ray: He has previously testified to that, without objection.

The Court: I think you should limit it to the time, lay the foundation for the conversation so that we can see if it was during the negotiations.

Q. I think your testimony was that from the time,—in the late thirties when you showed up at this property, discussions began respect the possibility of constructing this smelter at or near the site of this leased property, is that right?

(Testimony of John Davis Bradley.)

A. No, I said that we did not have discussions. I advised them of our progress, we did not have discussions with United if that is what you mean, we told them only of our progress.

Mr. Casterlin: ——I object to what he told them on the ground that no foundation is laid for a discussion of what was said and it would tend to alter the terms of the contract as drafted.

The Court: The objection is overruled.

Mr. Casterlin: It would not tend to interpret it and would invade the province of the Court.

The Court: Overruled.

Q. When did you talk to the people on the other side about the possibility of smelting, or local reduction?

A. We endeavored to keep United——

The Court: ——No, Mr. Bradley, just answer when. A. At numerous times. [106]

The Court: Commencing when?

A. Commencing in late '38 through '40, I will say late thirties and through the forties.

The Court: During any of these talks did you make any statements,—first, with whom did you talk?

A. My contacts with United were with *Mrs. Oberbillig* and *Worthwine*.

The Court: Did you ever talk with Mr. Oberbillig about the possibility of a smelter being constructed at the mine? A. Yes.

The Court: And when?

A. I don't recall precisely.

(Testimony of John Davis Bradley.)

The Court: About when?

A. The late thirties and through into the forties.

The Court: How late in the thirties?

A. Perhaps '38.

The Court: Do you recall any time in the forties before this contract was signed?

A. Specifically?

The Court: At the time you were negotiating this contract,—in 1941 was there any negotiations about it? [107]

A. Yes.

The Court: About what time, was it shortly before the contract was signed?

A. I think during the negotiations.

The Court: Over what period, we would have to have some idea?

A. Yes, 1940 and '41.

Q. When did the negotiations begin for this contract executed December 31, 1941?

A. As I stated previously, to the best of my memory, perhaps in the spring of '41, or it may have been before that.

The Court: After the spring of 1941, between that and the end of the year 1941, did you have any contact with Mr. Oberbillig or Mr. Worthwine about the possibility of a smelter being constructed at the site of the mine?

A. I don't think it would have been a point of discussion at that time.

The Court: No, I want to know was anything at all said or discussed.

A. My recollection is yes.

(Testimony of John Davis Bradley.)

The Court: Was anything said about who would build it or might build it?

A. I don't know that it was——

The Court: ——Not what was said, [108] but was anything said to Mr. Oberbillig or to Mr. Worthwine about who might build the smelter at the site of the mine.

A. May I put it this way, it was always assumed that the Bradley Mining Company would be the one that would build it if one was built. I would never enter a discussion by saying "We intend to build a smelter any certain year," but our work was progressing——

The Court: ——I asked was it discussed, about the possibility of one being built? A. Yes.

The Court: The maybe's of the situation were discussed? A. Yes.

The Court: And that referred to the possibility that the defendant here might build?

A. Yes.

Mr. Ray: I wanted Mr. Bradley to have before him a copy of the contract, it appears on Page 18 of the Circuit Court record, that is the portion I have in mind.

Q. (By Mr. Ray): Will you observe, Mr. Bradley, there in the first paragraph beginning on that page, "Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the [109] net smelter or reduction returns a fair charge for trucking from the mine to

(Testimony of John Davis Bradley.)

such smelter or reduction works." Now, was that provision discussed among you before this contract was signed?

A. Was it discussed before the contract was signed?

Q. Yes? A. Yes.

Q. When I say discussed, I mean with the other side? A. Yes.

Q. Was there any suggestion made that should reduction works be erected they would be erected by anyone except Bradley? A. No.

Mr. Ray: I have two letters, one identified as Exhibit Number 22, and the other as Exhibit 21, both letters from Mr. Worthwine.

The Court: I didn't get those numbers.

Mr. Ray: Number 21 and 22.

The Court: Exhibits 21 and 22?

Mr. Ray: Yes, your Honor.

Mr. Casterlin: We object to the introduction——

The Court: ——They have not been offered yet.

Mr. Ray: We want to offer [110] Exhibits Number 21 and 22 in evidence.

The Court: As I understand it, it is or can be stipulated as to the genuineness with respect to the letter. Can counsel stipulate that the letter was written on or about the date it bears and was signed by the person purporting to sign it and was mailed about the date it bears to the person to whom it is addressed?

Mr. Casterlin: And was received by the person?

(Testimony of John Davis Bradley.)

The Court: And was received by the person to whom it was addressed?

Mr. Casterlin: Yes.

The Court: Very well.

Mr. Casterlin: Now, as to Exhibits Number 21 and 22, we object on the ground that they are incompetent, irrelevant and immaterial. They pertain to a prior negotiation and show on their face that the contents of them or any dispute which arose under them were merged in the written contract of December 31, 1941.

The Court: I would like to see the exhibits, Mr. Clerk.

Mr. Brown: We have considered, your Honor, that these are very material in this case and are properly admissible for this reason: In the first place, they are corroborative of Mr. Bradley's testimony [111] with respect to the discussions had with representatives of the United Mercury with respect to the erection of a Bradley Mining Company smelter.

Secondly, Exhibit 5 in this case is the Option Agreement and the Agreement between the parties in 1939. In that contract it was provided that should local reduction of the concentrates become practical as determined by the Optionee; in other words, explicitly pointing out in that contract that the parties had in mind that it would be Bradley who built the reduction plant or have a reduction plant. The 1941 contract, while it mentions the smelter, did not define it as a Bradley smelter, yet,

(Testimony of John Davis Bradley.)

from his testimony and these corroborating letters of Mr. Worthwine's which particularly mentions the fact, if you and your family,—I don't worry about you and your family building a smelter, I am thinking in the future, if this at sometime passed into the hands of someone else——

The Court: ——It may be corroborative, I don't know whether there is any auxiliary issue on the subject yet or not. It may be that these letters are properly admissible if the plaintiff, on rebuttal, makes an issue or takes issue with what this witness has said,—this witness said that there was some discussion about the possibility of a smelter being built by Bradley's. [112] Now, the details of the negotiations are quite another matter. I don't know whether the plaintiff will make an issue on rebuttal with respect to that or not. If the plaintiff does, then these letters may become admissible as being corroborative of this witness' testimony. But until that time comes I feel that I should sustain the objection. If you want those letters incorporated as excluded evidence in the record under Rule 43c, you may do so.

Mr. Brown: We do want them included in the record.

[See pages 387-394.]

The Court: It is so ordered.

Q. Mr. Bradley, I think you testified concurrently with the production of tungsten which was not sold to the smelter, you produced antimony

(Testimony of John Davis Bradley.)

concentrates and shipped them to—first, when did you build the Bradley smelter?

A. We started construction in '48 and completed it in '49.

Q. It went into operation did it in 1949?

A. Yes.

Q. How long did it operate?

A. It operated until 1952.

Q. And what was treated in that smelter?

A. Antimony and gold concentrates.

Q. After you started the operation of that smelter did you, thereafter, sell any antimony concentrates? [113]

A. Yes.

Q. To outsiders? A. Yes.

Q. When and under what circumstances?

A. The circumstances were that the smelter was not performing too well and we had concentrates backed up ahead of it, and secondly, it was of interest to us to verify and confirm our settlement provisions with the United Mercury mines.

Q. What record was kept, if any, of the amount of concentrates that went into the Yellow Pine smelter?

A. The same record that was kept of the concentrates being shipped off the property to other smelters, which was, namely, by weight and quality control.

Q. Were the concentrates produced at your mine brought to the smelter by truck?

A. Yes, they were brought from the concen-

(Testimony of John Davis Bradley.)

trator to the mouth of the roasters by truck, but it was only a distance of approximately fifty feet, the reason being so that we could weigh on the truck scales the same as if the concentrates were being shipped to the rail head.

Q. So that you kept and maintained records of all of the concentrates that went into the smelter?

A. Yes sir.

Q. Was the amount of concentrates shipped to the outside [114] substantial as compared to the amounts of concentrates treated?

A. Yes sir.

Q. And over what period of time were you selling concentrates to the outside?

A. Over the entire period of time the smelter was operating. I must qualify a previous answer if I may. I mentioned that the antimony,—that we had made some spot shipments. However, during that same period of time we were shipping half of our gold concentrates to the Tacoma smelter.

Q. You smelted substantially all of your antimony concentrates? A. Yes.

Q. But you sent approximately half of your gold concentrates to Tacoma? A. Yes.

Q. Why did you divide the gold concentrates between your own smelter and the Tacoma smelter?

Mr. Casterlin: I object to the question as being incompetent, irrelevant and immaterial, and throwing no light on the issues involved here.

The Court: I can't determine yet whether it is

(Testimony of John Davis Bradley.)

or not, I will overrule it, it calls for a reason, doesn't it?

Mr. Ray: Yes, your Honor.

The Court: He may answer. [115]

A. The reason being twofold, one, we couldn't ship all of the gold concentrates to outside smelters and were limited to approximately 50%, therefore, we had to design our antimony plant to accept the other 50% of the gold concentrates.

The Court: Why couldn't you ship them all out?

A. The reason we couldn't ship them all out was owing to the high arsenic and antimony content in the gold concentrates and other smelters refused to accept such a heavy tonnage of gold concentrates.

The Court: Because of that content?

A. Yes, because of the arsenic and antimony in the gold concentrates.

The Court: And what effect would that have?

A. The concentrates were going to Tacoma and arsenic becomes a miserable impurity to remove and we cluttered up their entire circuits, getting into their copper and into their lead and every other metal, so that when our shipment with arsenic that was running several percent became too heavy they forewarned us, so that we had to make our plans for the antimony smelter to accept those, so we devised a metallurgy to keep our slag in balance and which required about half of the tonnage so it worked out satisfactorily [116] in either case, except in the case of our smelter it didn't work out satisfactorily overall economically.

(Testimony of John Davis Bradley.)

Q. Now, on the gold concentrates shipped to Tacoma, did you receive compensation from Tacoma? A. Yes.

Q. In what form, what did you call it?

A. Net smelter returns.

Q. Did you compute royalties due to the Plaintiff on the basis of those net smelter returns?

A. Yes.

Q. How did you compute the royalties paid on account of the gold concentrates treated in the Yellow Pine smelter?

A. On exactly the same basis as the net receipts from the American Smelting and Refining Company, except in the beginning we did not deduct any freight so that the United Mercury Mines benefitted substantially.

Q. How did you compute the royalties on the antimony concentrates treated in the Yellow Pine smelter?

A. On the basis of past practices of antimony shipments.

Q. To outside smelters?

A. To outside smelters.

The Court: When you shipped these gold concentrates to Tacoma did you receive payment for them? A. Yes.

Q. And did you compute royalties to the plaintiff on the basis [117] of five percent of what you received? A. Yes sir.

The Court: Did you report that account to the Plaintiff?

(Testimony of John Davis Bradley.)

A. Yes, on a monthly basis.

The Court: And did you explain that transaction?

A. Yes.

The Court: Is there any issue as to that?

Mr. Casterlin: On what was shipped to outside smelters?

The Court: To Tacoma.

Mr. Casterlin: No, there is no issue on that.

The Court: Over what period did that occur?

A. To Tacoma, that would have gone even prior to the construction of the smelter, right to the shut-down of the property in 1952, so it would probably be from 1946 to 1952.

The Court: On how many occasions did this type of transaction occur, that is, where you shipped gold concentrates to Tacoma, paid, and you would compute the royalty and report to the Plaintiff?

A. We were shipping concentrates at the rate of about 2,000 [118] tons a month, so it would occur about every day that we were shipping carloads of concentrates.

The Court: Then it would occur more than one time a week?

A. Yes, oh, yes.

Q. Did you report a basis for computing the royalty on antimony concentrates, — I don't mean antimony concentrates, — gold concentrates, that went through your own smelter and make those reports to the Plaintiff at the same time that you

(Testimony of John Davis Bradley.)

were making your reports on the concentrates that went to Tacoma?

A. On the same basis and at the same time.

Q. At the same intervals that you were reporting your own gold concentrates to Tacoma?

A. All throughout the operation of the smelter antimony concentrate returns were submitted to the United Mercury.

Q. Did you report to the Plaintiff your computation on account of antimony concentrates that were treated in your own smelter?

A. Yes, we reported to the Plaintiff.

Q. That was beginning then in August of 1949, and continuing until 1952? A. Yes.

Q. Did the defendant compute and pay royalties in accordance with that method on all the concentrates, the antimony [119] concentrates that were ever treated by the Yellow Pine Smelter?

A. Yes.

Q. Mr. Bradley, if you please, was there ever any modification or supplement to the contract of December 31, 1941?

A. Yes, there was a supplemental agreement negotiated in 1950.

Mr. Ray: There has been identified in the record, a document, being Exhibit Number 6, I want to have it identified in this record. The Exhibit 6 is attached to the affidavit of John H. Bradley, dated 10-10-1951.

The Court: According to my notes, Exhibits 1

(Testimony of John Davis Bradley.)

to 7 are in the Clerk's file, I don't know where they are, do you have a copy of it?

Mr. Ray: I have a copy.

The Court: Do you agree on the genuineness of the document?

Mr. Casterlin: We will raise no question of the genuineness of the copy.

Q. Mr. Bradley, are you familiar with Exhibit Number 6? A. Yes, I am.

Q. Is that a copy of the contract that we just referred to? A. Yes, it is.

Q. Who are the parties to that agreement?

A. The Bradley Mining Company, United Mercury Mines and O. W. Worthwine.

Q. Who negotiated that contract on behalf of the Bradley Mining Company? A. I did.

Q. And with whom for the other side?

A. It was with *Mr.'s* Worthwine and Oberbillig.

Q. Who prepared the draft of that contract?

A. Mr. Worthwine.

Mr. Ray: We offer Exhibit 6 in evidence.

Mr. Brown: That appears on Page 66 of this record (indicating).

The Court: Do you wish to state the purpose of the offer?

Mr. Ray: Yes, your Honor, we think it is important in connection with our defense in that it shows the interpretation by the parties of what the contract means, on the royalty basis, the computation of royalties.

The Court: Are you relying on the recitals in

(Testimony of John Davis Bradley.)

the Whereas clauses as being a substantive interpretation of the contract?

Mr. Ray: Yes, your Honor, stating that we have paid royalties to a certain time.

Mr. Casterlin: Royalties on what transaction?

The Court: I notice in the next to last [121] Whereas clause it says: "The said Bradley Mining Company did, on the 20th day of June, 1950, pay to the United Mercury Mines Company and said Oscar W. Worthwine, the royalties due for the month of May, 1950." Is that what you are relying upon?

Mr. Ray: Yes, your Honor.

The Court: I was wondering about the purpose of this myself, but apparently the purpose is in the next to the last Whereas clause.

Mr. Ray: There is another provision in there, too, your Honor, it is on Page 69.

The Court: 69 of the Transcript?

Mr. Ray: Yes sir. "It is further agreed that the said Bradley Mining Company shall make the usual monthly reports as to money received by it during the preceding month upon which royalties would be payable, stating the amounts of royalties that had accrued, but, instead of sending the check as has been the practice during the past ten years shall make a notation thereon to the effect that the above accrued royalty has been postponed." Now, that is the agreement that we continued to do it.

The Court: Emphasizing the word 'usual'.

(Testimony of John Davis Bradley.)

Mr. Ray: Yes, your Honor, and [122] that is written by the other side.

The Court: But that doesn't appear here.

Mr. Ray: The witness just stated that it was written by Mr. Worthwine.

Mr. Casterlin: May I ask a question?

The Court: You may.

Q. (By Mr. Casterlin): You say that in 1950 Mr. Worthwine was representing Mr. Oberbillig, is that correct? A. Yes sir.

Q. And at the same time he was representing you as local counsel, was he not? A. Yes.

Q. When did he first start representing you as local counsel, was it before December 31, 1941, or was it after? As a matter of fact, hasn't Mr. Worthwine been doing work for you, and representing you and your family since about 1929 or '30?

A. No.

Q. When did he start representing you?

A. I don't think that we had a representative, as such, Mr. Casterlin. Mr. Davis was our San Francisco attorney, our family, company attorney, and I don't believe that we designated Mr. Worthwine, even as our Idaho counsel, until [123] Mr. Davis got tied up in the war. I was trying to recollect, I wasn't trying to dodge the answer, until Mr. Davis left San Francisco and went to Washington we looked to him, naturally, for all of our legal work. It came about that after he left Mr. Worthwine took on the Idaho load without really clearing, at times, with Mr. Davis, owing to his absence.

(Testimony of John Davis Bradley.)

Q. He was your attorney at the time this 1950 contract was drawn?

A. Yes, he was acting as our local counsel. I think it would have been submitted to Mr. Davis in 1950 for confirmation, however.

Mr. Casterlin: I think I will object to this as incompetent, irrelevant and immaterial, it tends to alter the terms of a written contract. It purports to be merely an extension of time of payment of royalties under the original contract and, therefore, whatever terms are used would have reference to the original contract and simply be a postponement of the royalties required to be paid by the original contract.

The Court: It seems to me that the objection goes to the weight rather than the admissibility of this. The objection will be overruled and Exhibit Number 6 will be admitted in evidence. [124]

[See pages 377-381.]

Q. (By Mr. Ray): Mr. Bradley, the contract just referred to, Exhibit Number 6, provides for the suspension of royalties payments for a time, does it not? A. Yes.

Q. Were those royalties that were suspended ultimately paid? A. Yes.

Q. Did you, during the month following the execution of Exhibit Number 6, make a report to the plaintiff showing what royalties had accumulated and would have been paid except for this suspension? A. Yes, we did.

Q. Now, you have testified that Mr. Worthwine

(Testimony of John Davis Bradley.)

participated in and wrote this agreement. He was a party to the agreement itself, wasn't he?

A. Yes.

Q. And he was a participant in the royalty, isn't that so? A. That is correct.

Q. Up until the time you prepared Exhibit 6 in July of 1950 had Mr. Worthwine ever objected to the method by which you computed royalty on the concentrates treated in the Yellow Pine Smelter?

A. No, he had not.

Q. Has he ever to this day objected to it?

A. No, he has not. [125]

Mr. Casterlin: Now, I move to strike the answer for the purpose of objection.

The Court: State your objection, Mr. Casterlin.

Mr. Casterlin: The objection is that Mr. Worthwine might have been dealing with his own interests, it is not shown that he had any authority to deal with the royalties that were coming from Bradley to the United Mercury.

The Court: Your objection goes, not that he was not acting in his own interest,—

Mr. Casterlin: —No.

The Court: —but that it was his own interests and not the interest of the plaintiff, that there was no showing of authority, did I understand?

Mr. Casterlin: Yes.

The Court: The objection is sustained and the answer may be stricken. The motion to strike the answer is granted.

Q. Mr. Bradley, did Mr. Oberbillig, or anybody

(Testimony of John Davis Bradley.)

representing the United, ever object to the method in which you had been computing the royalties on the materials that went through the Yellow Pine smelter?

Mr. Casterlin: We object to that on the grounds that it is a dual question—no, I will withdraw [126] the objection.

The Court: Will you read that question for me, Mr. Reporter.

(Question read by Reporter.)

Mr. Casterlin: I have withdrawn my objection.

The Court: Very well, the witness may answer.

A. No, not until 1951.

Q. When, if you recollect in 1951?

A. I don't recollect, maybe it was mid-year, but I don't recall.

Q. Mr. Bradley, to your recollection, was the first objection ever made by the plaintiff, in 1951?

A. Yes.

Q. At that time had you been computing and paying the royalties for approximately two years?

A. Yes.

Mr. Ray: We are nearing the end of our examination, your Honor, and I wonder if we might have the indulgence of the Court for a few minutes.

The Court: Yes, we will take a five minute recess.

March 19, 1957, 4:25 o'clock p.m.

Q. Mr. Bradley, in answering questions put to you by His Honor you spoke of the economic neces-

(Testimony of John Davis Bradley.)

sity of mine products being [127] concentrated, because of the cost of shipment, before they were shipped to the consumer or the smelter, is that so?

A. That is so except in unusual cases where the ore is sufficiently highgrade that it will stand the freight.

Q. Is it customary throughout the mining industry for mines to be equipped with some sort of concentration facilities? A. Yes.

Mr. Casterlin: We object to that unless it is confined to the area where the property is situated.

Mr. Ray: I said throughout the industry, including Stibnite.

The Court: Overruled.

A. If it is any size mine at all it would normally have a concentrator on it.

Q. In the industry can you state whether or not the number of mines outnumber the number of smelters? A. By a wide margin.

Q. Is it economical in the mining industry for the ordinary mine to be equipped with a smelter?

A. For the ordinary mine to be equipped with a smelter?

Q. Yes.

A. No, it is not, may I cite an example.

Mr. Casterlin: I will stipulate that is a fact.

Mr. Ray: If you stipulate that [128] is a fact, very well.

Q. What did it cost to construct the Stibnite smelter?

(Testimony of John Davis Bradley.)

Mr. Casterlin: That is objected to as incompetent, irrelevant and immaterial.

The Court: What is the purpose of that?

Mr. Ray: I think there is a rule of law, your Honor, that in construing a contract if the meaning is uncertain that the contract will be construed in view of all the significant facts and there will not be given a construction which works a hardship on one party and unjustly enriches the other.

The Court: But this smelter didn't exist at the time this contract was formed.

Mr. Ray: That is true, but we contend that the parties never intended, and the circumstances show, that they never intended that the plaintiff should get a five percent royalty on concentrates after smelting costs had been deducted if they go to Tacoma, but that they would get the smelting free if it goes to the Yellow Pine.

The Court: There is no contention here that the Plaintiff ask that this smelter be constructed, is there?

Mr. Ray: I understand that, but it was. [129]

The Court: I suppose that the defendant constructed it in its own interest, the fact that it may have redounded to the plaintiff's interests also is immaterial here.

Mr. Ray: The contract doesn't provide that there shall be two rates of royalty, one if the concentrates were treated in one place, and one if they were treated in another.

The Court: The objection is sustained. If you

(Testimony of John Davis Bradley.)

wish the answer in the record under the excluded evidence rule, you may have the answer.

Mr. Ray: I would like to have him answer that question as to what it cost.

A. Approximately two million dollars, including homes for a few of the smelter workers.

Q. And who paid that amount?

A. The Bradley Mining Company.

Q. Who operated it thereafter?

A. The Bradley Mining Company.

Q. Who put up the operating expenses?

A. The Bradley Mining Company.

Q. And what did they amount to?

Mr. Casterlin: I think now that we are getting into the operating expenses, and I object to that as incompetent, irrelevant and immaterial, and not within [130] the purview of the first question.

The Court: I assume this is all excluded evidence under the rule, though some of it I would admit. I would admit the evidence as to who paid the operating expenses.

Mr. Ray: And how much they were.

The Court: That is the next question.

Mr. Ray: Yes.

The Court: And that would be excluded evidence.

Mr. Ray: Very well.

A. Approximately a million and a half a year, for the smelter alone.

The Court: Does that terminate the evidence excluded?

(Testimony of John Davis Bradley.)

Mr. Ray: That is all of that.

The Court: Then all of that with respect to the construction of the smelter, except the statement that the defendant paid the operating expenses, will be excluded evidence under the rule.

Q. Mr. Bradley, does the word, the term 'gross royalty from ores mined' have an understood meaning in the mining industry?

A. Yes, I feel that it does.

Q. What does it mean? [131]

Mr. Casterlin: I object to that as being an interpretation of the contract on the part of one party.

The Court: The objection will be sustained to the question in that form, and you may rephrase it tomorrow morning. We will recess until ten o'clock.

March 20, 1957, 10:00 o'clock a.m.

Mr. Ray: Shall we proceed, your Honor?

The Court: Yes, I believe that Mr. Bradley was still on the stand.

Q. (By Mr. Ray): Mr. Bradley, there is a question I would like to ask you in the interest of clarification. You testified yesterday that there were certain products which at one time went to the mint and at other times went to smelters and at other times went to purchasers other than smelters. Now, was it the value or the character of the product that determined where it went?

A. Principally the character .

Q. And you testified with respect to tungsten that it had that character that required it to go to

(Testimony of John Davis Bradley.)

places other than smelters? A. Correct. [132]

Q. Would you testify now, please, as to relatively what was the importance of tungsten as compared to the other products produced during the several years next following January 1st, 1942?

A. Tungsten was by far the predominant product.

Q. Tonnage wise or dollar wise?

A. Definitely dollar wise, but I think also tonnage wise.

Mr. Ray: If the Court please, yesterday we offered Exhibit 5 A, and it was excluded. Your Honor permitted me to ask questions which would be embraced in rejected evidence. With your Honor's indulgence I would like to pursue that matter a little further.

The Court: Now, you are resuming the record of excluded evidence now under Rule 43 c with respect to Exhibit Number 5 A.

Mr. Ray: That is correct, if I may.

The Court: You may.

Mr. Ray: I would like to have the witness handed this document.

Q. Will you examine Exhibit Number 5 A, Mr. Bradley, and tell me whether it contains a provision covering net smelter returns?

A. Yes, it does. [133]

Q. Does it contain a provision covering net mint returns? A. Yes.

Q. Does it contain a provision covering net rev-

(Testimony of John Davis Bradley.)

enue as we have been speaking about it in this case, as it was submitted to you?

A. As submitted to me it covered net mill returns.

Q. I want you to state whether or not it contained a net revenue clause?

A. As submitted to me it did not.

Q. But it did contain a clause respecting net mill returns, will you read that?

A. "By net mill returns, as used herein, is meant the net amount paid by any milling company, with the right of said milling company to deduct milling charges only."

Q. During your discussions with Mr. Worthwine respecting that draft, what was done with that 'net mill returns'?

A. That became the net revenue clause.

Q. You mean by that that it was deleted from the draft?

A. Yes 'net mill returns' was deleted.

Q. And there was substituted for it the net revenue clause? . A. Yes sir.

Q. Written in your handwriting?

A. Yes sir.

Q. Did you then explain to Mr. Worthwine why you suggested the change from net milling to net revenue?

A. I am sure that I must have. [134]

Q. What did you state?

A. Well, number one, we had a product that didn't answer net smelter or net mint, and net mill

(Testimony of John Davis Bradley.)

didn't seem to me to be the proper definition for it. That product, of course, being tungsten.

Q. There wasn't tungsten in '39, was there?

A. No. I beg your pardon, in 1939 there was no tungsten.

Q. Was there mercury?

A. There was mercury. There were indications that there might be other minerals that wouldn't come under the net mint or net smelter.

Q. And was that the reason that you suggested the substitution of net revenue clause for net milling clause?

A. We were hunting for a clause that would cover products that would not go to a mint, such as gold bullion, or sulfide concentrates that would go to a smelter.

Mr. Ray: Now, I have concluded my offer, your Honor, with respect to excluded evidence.

The Court: Very well.

Mr. Ray: And with that I would like to renew my offer of Exhibit 5 A.

The Court: At this point the record may show that the evidence respecting the excluded evidence under the rule is terminated as to the offer of Exhibit 5 A. You now renew the offer of the exhibit?

Mr. Ray: Yes, your Honor, we renew our offer.

Mr. Casterlin: We renew our objection.

The Court: What is the purpose of the offer?

Mr. Ray: The offer is to show that the reason for the inclusion of this net revenue clause in the 1939 agreement was to take care of the products

(Testimony of John Davis Bradley.)

that would not go to a smelter or mint and be subject to net mint or net smelter returns.

The Court: Exhibit 5 A never came into being as a legally effective document.

Mr. Ray: No, but the net revenue provision that appears in Mr. Bradley's handwriting on Page 3 did come into both Exhibit 5 and Exhibit 7, in Exhibit 5 first and then it was retained in Exhibit 7.

Mr. Casterlin: The dilemma that we are in now is that they have some evidence in here that possibly might be admissible and some which would not be admissible, and the portion which is not admissible, not being objected to at the time the evidence was offered,—if that was segregated I am sure there would be some that we would have no objection to.

The Court: You mean of the testimony in the record which has just been made of excluded evidence. [136]

Mr. Casterlin: Yes.

The Court: What do you have in mind, Mr. Casterlin, withdrawing your objection to some of it?

Mr. Casterlin: No, not as the record now stands.

The Court: I don't know just what you have in mind at this time.

Mr. Casterlin: The situation is just this, your Honor, when they were offering evidence which was denied, now, if the ruling is changed and admits it then we have been deprived of our right to object to certain phases of it.

The Court: I probably misunderstood you, I

(Testimony of John Davis Bradley.)

thought there was a suggestion by you that some of the evidence in the record of excluded evidence might be admissible.

Mr. Casterlin: That is right, your Honor, if it is offered not as a part of the denied evidence, but it was all offered during the offer made of denied evidence.

The Court: As to what part, Mr. Casterlin, do you have no objection?

Mr. Casterlin: I think I will let the record stand just as it is. [137]

The Court: I take it that the defendant offered the evidence anticipating the ruling heretofore made by the Court and offered it as excluded evidence. Now, if there is no objection to any part of it I will receive it.

Mr. Casterlin: We do have objection to parts of it.

The Court: Is there part you have no objection to?

Mr. Casterlin: I think we will let the record stand and probably bring the matter back in in another way.

The Court: The record will stand as now made, you have a record of excluded evidence. The objection is sustained. It seems to me that the question regarding Exhibit 5 A, after the admission of Exhibit 5, it seems just an attempt to bring in surrounding circumstances one step removed, circumstances surrounding the execution of the contract of 1939, Exhibit 5, to aid in the interpretation of

(Testimony of John Davis Bradley.)

the 1941 contract or agreement, which as I recall, is Exhibit 7.

Mr. Ray: It was my purpose, and I don't want to argue a matter after the ruling of the Court, but there was a reason which both parties recognized for bringing that into their dealings. That was the particular [138] purpose, it was to reach a particular goal, that provision, the net revenue clause. Prior to that time they were operating under a contract of net profit, which had nothing to do with smelter returns or mint returns, or anything else, and they were shifting to a new type of agreement, and this new type of agreement, as submitted, contained the mint return and smelter return clause, and it contained a mill return clause, which Mr. Bradley testified in the custom of his trade would not meet certain products that they were or might be producing. Therefore, the parties agreed that it was necessary to introduce something into this contract which would take care of mercury or other products which wouldn't go to the mint or the smelter. That was the purpose of its introduction,—that was the reason they agreed to eliminate the milling clause, and insert the net revenue clause. Now, when you get into that meeting with Mr. Bradley and Mr. Worthwine at that discussion, then, you are in the circumstances out of which the contract grew.

The Court: Out of which the 1939 contract grew.

Mr. Ray: Yes, and that was carried over into the 1941 contract.

The Court: That is a matter of argument, the

(Testimony of John Davis Bradley.)

ruling stands with respect to Exhibit 5 A, [139] the objection is sustained.

Q. Mr. Bradley, does the smelting process add value to the products of the mine? A. Yes.

Q. Will you explain that briefly?

A. Well, the——

Mr. Casterlin: I object to this on the ground that it is incompetent, immaterial and irrelevant as to the value of the mines or the minerals in view of the fact that Bradley is the owner of the mine, the owner of the minerals that are in the ground and the United Mercury has no interest in those at all. This would be immaterial and would constitute a self-serving declaration.

The Court: And what would be the purpose, Mr. Ray?

Mr. Ray: This is introductory to some questions with respect to the uniform practices and customs in the industry.

Mr. Casterlin: Now, Mr. Ray, I understand that there is a little dispute here. At any rate, I am not clear as to your position, in one instance you have stated that this net revenue clause is not according to the custom in the industry and is peculiar to this situation. [140]

Mr. Ray: I said it was not a standard clause frequently found in use in the industry, but was brought into the contract to take care of this particular situation.

Mr. Casterlin: Yes, and in another instance you

(Testimony of John Davis Bradley.)

introduced evidence as to custom with respect to this same subject matter.

The Court: What is the purpose of this, there is no objection and nothing before the Court.

Mr. Casterlin: I realize that, your Honor, and I suppose that I am out of order and I apologize to the Court. My question of Mr. Ray was for the purpose of objecting to certain testimony, questions that might be asked if I knew the theory on which they were proceeding.

The Court: You made the inquiry as to the purpose and this statement was made by Mr. Ray that it was preliminary to show the practice.

Mr. Ray: That is correct.

The Court: There was an objection, as I recall now, to the last question. Will you read the question, Mr. Reporter?

(Question read by reporter.)

The Court: The objection is overruled [141] and he may answer.

A. You are taking, in effect, a crude material that is very close to its native state, still containing gang materials, impurities such as arsenic, sulphur and so forth. The product from the mine, being the product from the mine and the concentrator not having any use, whereas the end product after smelting and refining having a use, it being reduced down to its final state for manufacturing purposes. An example in case of antimony is the history and practice of the trade has been that the ore or con-

(Testimony of John Davis Bradley.)

concentrates is approximately one-half of the value of the finished product.

Q. Mr. Bardley, within the mining and smelting industry would the expression "the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs", within the usage of the industry, would that expression be recognized as included within those values,—the values added to the product by refining in a smelter?

Mr. Casterlin: I will object to that question as invading the province of the Court and calling for an answer to the ultimate question here.

The Court: Sustained. You may make a record of excluded evidence as to that if you desire. [142]

Mr. Ray: I would like to make a record, your Honor.

The Court: You may answer, Mr. Bradley, and the answer will be in the record of excluded evidence.

A. May I have the first portion of that question again?

Mr. Ray: I will restate the question if I may?

The Court: You may.

Q. Within the mining and smelting industry, according to its customs and practices, would the expression "the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs," be considered

(Testimony of John Davis Bradley.)

as included the values added to the mined products by refining in a smelter?

A. Definitely not.

Mr. Casterlin: And to that we renew the same objection.

The Court: And the same ruling,—the answer may come in and be in the record of excluded evidence.

A. The answer is in the negative.

Mr. Ray: There is a further question I would like to ask, your Honor, and I don't [143] know what your Honor's ruling will be, but it is kin to this.

Q. I am referring, Mr. Bradley, to the provisions of the Revenue Code, Section 114 (b)(4)(B), the 1939 Code, which relates to the depletion. I read this language: "As used in this paragraph the terms 'gross income from the property' means the gross income from mining." Would you say whether or not that language reflects, and is in harmony with, the customs, practices and usage in the mining industry? A. Yes.

Mr. Casterlin: I interpose the following objection: by the language of the statute the definition is confined to the particular act for revenue purposes only and revenue is not an issue here. The second ground is that it invades the province of the Court and the third ground, the witness is not qualified to interpret the statute.

Mr. Ray: I am not asking for an interpretation

(Testimony of John Davis Bradley.)

of the statute, I am asking if that language is in accord with with the custom, usage and practice.

The Court: The objection is sustained but the answer may stay in the record as a record of excluded evidence.

Q. At the time the 1941 agreement was written, was there any particular reason of recent occurrence for the inclusion [144] in the 1941 contract for the net revenue clause? A. Yes.

Q. What was that reason?

A. The discovery of tungsten and the knowledge of mercury in the district.

Mr. Casterlin: Is this going in under the excluded evidence rule?

Mr. Ray: No, sir.

The Court: It is only this question, there was no objection made to the last question.

Mr. Casterlin: I was just wondering whether it was asked under the excluded testimony rule.

The Court: Do you desire to make an objection?

Mr. Casterlin: What was that question?

The Court: Read the question, Mr. Reporter.

(Question read by reporter.)

Mr. Casterlin: No, I have no objection.

Q. Mr. Bradley, are the terms "gross royalty" and "net royalty" frequently used in the mining and smelting industry?

Mr. Casterlin: We object to that on the ground that it is not shown that there is any ambiguity or uncertainty in the terms.

Mr. Ray: I am not addressing myself [145]

(Testimony of John Davis Bradley.)

at this time, if the Court please, to the contract. I am addressing myself to the two letters which occur on Page 180 and 181 of the transcript, received in evidence.

The Court: What are those letters, what are the exhibits?

Mr. Casterlin: They are two letters which were submitted and I think, as counsel says, they appear on Page 180 and 181.

The Court: They are here as a part of this record as Exhibits 26 and 26A.

Mr. Ray: Yes, your Honor.

The Court: The terminology used in those letters, you are asking the witness if those terms have any special signification in the mining and smelting industry.

Mr. Ray: My position is that they appear in the two letters, they appear as net in one place and gross in the other, and we take the position that we have a right to explain what is understood and what those terms mean in the mining industry.

The Court: Wouldn't it be a necessary foundation first to ask him whether at that time these terms had any specific signification in the mining industry, with mining men or in the mining industry generally?

Q. I call your attention, Mr. Bradley, to Exhibit Number 26, [146] which is a letter addressed by you to Mr. Oberbillig and Mr. Dorsey, dated January 29, 1942, and also another letter dated March 17, 1947. At either or both of those times

(Testimony of John Davis Bradley.)

were the terms net royalties and gross royalties terms in common use and practice in the mining industry? A. Yes, sir, they were.

Q. How were those terms understood by the mining industry?

Mr. Casterlin: I object to that question on the ground that it is not a question of how a simple expression which is common to all commercial economic activities is understood in the mining industries.

The Court: Stated in that form, it seems to me that it would be necessary to first show that those terms had some special signification apart from their everyday meaning, in the mining industry.

Q. Did the term "net royalty" have some special significance in the mining industry? A. Yes.

Q. What was that special significance?

A. When one sort of looks at the word "net" without any qualification it was normally assumed that it was on the sharing of the profits.

Q. And what is a gross royalty?

A. A gross royalty would be tied to the income from the mine itself, the net returns from the sale of the ore or concentrates. [147]

Q. Without regard to profit?

A. Without regard to profit.

Q. Now, what is the net sale?

Mr. Casterlin: Before you go to the next question,—I now move to strike the answers to the last two questions on the ground that it is now evident

(Testimony of John Davis Bradley.)

that the term net and the term gross are common to all commercial transactions.

The Court: Perhaps as to net, but not as to gross. As I understood the witness, gross doesn't really mean that, it means after certain processes have taken place. I presume it is just another way of saying that it is the returns from the first marketable product. The motion will be granted. Do you wish, Mr. Ray, that testimony to stay in the record under the Rules as excluded evidence?

Mr. Ray: Yes, please.

The Court: Very well, it may be in the record as excluded evidence under the Rule.

Mr. Ray: May we have a short recess at this time, we may have nothing further to offer.

The Court: Yes, we will take a short recess, five minutes [148]

March 20, 1957, 10:45 O'Clock A. M.

Mr. Ray: If the Court please, I have handed Mr. Bradley a copy of the Transcript of the Record, I take it that is permissible.

The Court: You mean the record in the Court of Appeals?

Mr. Ray: Yes, I want to ask him some further questions which I assume is in pursuit of excluded evidence, and I am going to refer to Page 180 and 181.

The Court: Now, you are referring to some other correspondence?

(Testimony of John Davis Bradley.)

Mr. Ray: I am referring to the letters that I referred to a few moments ago.

The Court: Which are a part of Exhibits 26 and 26A?

Mr. Ray: Yes, your Honor.

The Court: So when you are referring to transcripts you are really referring to Exhibits 26 and 26A.

Mr. Ray: That would be correct.

Q. Mr. Bradley, in Exhibit Number 26, you refer to a 5% royalty on net sales proceeds and in Exhibit 26A you refer to a 5% gross royalty?

A. Yes.

Q. In the practice and custom of the mining industry is there any difference between a 5% royalty on net sales and a 5% gross royalty?

Mr. Casterlin: I understand this is under the Rule?

Mr. Ray: Yes.

A. No.

Q. Will you explain what, according to the practice and usage in the mining industry, each of those mean?

A. All reference to royalties in the instance of mining refers to royalty on the value of the mined product, and you attach the amount, which in this case is 5%, and it is all under the theory,—the broad theory of net smelter returns, whether it be stated as net sales proceeds or as gross income from mining. The gross in mining language ap-

(Testimony of John Davis Bradley.)

plies to the sales, the net sales returns, the net sales returns taken from the mining property.

Q. Before or after smelting and refining?

A. Definitely before any processing that would change the character of the product. In mining parlance you are either talking about ore that is high enough in grade to ship or an ore that has to be concentrated to make it shippable, but you never talk about a smelted product when you talk about royalties, I never heard of such a thing. [150]

Mr. Ray: Now, your Honor, that is the end of the excluded evidence.

Q. Mr. Bradley, would you now turn to Page 17 of the Transcript and you are now referring to Exhibit 7, the contract of December 31, 1941, and I call your attention particularly to the words in the second paragraph: "Produced from said properties." In the customs and practice of the mining industry is there a recognized meaning for the words "produced from the properties?"

A. Yes, sir, that is——

Mr. Casterlin: ——I submit that the question has been answered.

Q. What is the recognized meaning?

Mr. Casterlin: I object to this question until it is first shown that there is some uncertainty and ambiguity in the language, which is contained in the contract of December 31, 1941, or until it is shown that there is some peculiar meaning in the mining industry which is not common to other practices.

(Testimony of John Davis Bradley.)

The Court: It would seem to me that it would be first necessary to lay the foundation to show that the terminology in the mining industry means something different or apart from the everyday and ordinary signification of the words. [151]

Mr. Ray: Perhaps I can ask a preliminary question.

Q. Mr. Bradley, in 1941, when this contract was entered into, what did the property consist of?

A. The properties covered by the agreement included such mining claims,—some were patented and others were unpatented, they were, mining facilities and concentrating facilities and of course, homes and schools.

Q. Was there any smelter there? A. No.

Q. Now then, in the mining industry does it sometimes occur that there are smelting facilities upon mining ground? A. Yes.

Q. And sometimes there are not smelting facilities on mining ground?

A. That is correct.

Q. Are there occasionally situations in the mining industry in which, in addition to all mining facilities, there are some other facilities which is not smelting but still outside of the area of mining? Some process that might not be strictly smelting, but also is not mining, such as the leaching of concentrates and that sort of thing?

A. Well, I was trying to catalog your question, Mr. Ray. By the Revenue Code, it is either one way or the other, and you do have some marginal

(Testimony of John Davis Bradley.)

points, I grant, such as [152] cyaniding, quicksilver and leaching, that are specifically mentioned as includable, and certain forms of roasting ahead of cyanidation that are all a part of mining.

Q. Now, where your properties include no smelting or refining facilities, what, in the practice and customs of the mining industry, is included within the words "products of the property?"

Mr. Casterlin: Now, I object to that on the ground that it is incompetent and irrelevant, and proper foundation has not been laid. The contract itself shows that this mining ground is owned by Bradley and the evidence in this case also shows that this net revenue clause was inserted in here at his request, in Bradley's own handwriting, and consequently it would be self-serving.

The Court: The evidence does not so show, Mr. Casterlin, as to these exhibits.

Mr. Casterlin: Then I will withdraw that portion of the objection. Yes, that is right, your Honor.

Mr. Ray: The contention is made by the Plaintiff that the proceeds from the property include not only the value of the product taken from the mining property but the refining and smelting.

The Court: Yes, I understand, but let's determine whether this term has some special signification or connotation in the mining industry other than the everyday meaning of the word. It seems to me to be immaterial. Now, when mining men refer today to mining, that may be a term of spe-

(Testimony of John Davis Bradley.)

cial connotation, that is, in the mining industry. It may include certain steps and may not include other steps. Now, if that is what you want to show.

Mr. Ray: I thought that is what I was asking.

Q. Mr. Bradley, does that have a particular meaning in the mining industry?

A. Does what have a particular meaning?

Q. Products produced from the mining property? A. Yes, it does.

Q. As distinguished from the product of a shoe factory or a dairy? A. Yes, I would say so.

Q. And what is that peculiar meaning that it has in the mining industry?

A. Produced or taken from a mining property means extracted and, perhaps, concentrated, or, in the instance of the Yellow Pine where we had different types of ores, oxidized, we had leaching, roasting, some cyaniding, in addition to flotation [154] concentration, specific gravity work, we had the whole gamut. I am not certain that I have answered your question, Mr. Ray.

Q. What does that, taken from the property, what does that mean, produced from the property?

Mr. Casterlin: I object to this on the ground that it is a self-serving declaration and invades the province of the court. Those words are all simple.

The Court: They may be simple, Mr. Casterlin, but they may have some particular meaning in the mining industry.

Mr. Casterlin: But that simple phase in here "produced from said properties", that has no pecu-

(Testimony of John Davis Bradley.)

liar meaning aside from the generally accepted meaning of the terms.

The Court: That isn't the question being asked now.

Mr. Ray: He has testified that the phrase does have a special meaning and I am asking him now what it is.

The Court: The objection is overruled, he may answer that.

Q. I think you have stated, Mr. Bradley, with respect to your property that the meaning of 'produced from the property' meant extracted from the property plus certain things? [155]

A. Yes.

Q. Now, did it include anything beyond those certain things?

A. Produced from the property means to me, mining or extraction and, if necessary, concentration.

The Court: Not what it means to you, what it means in the mining industry generally, or what did it mean at that time.

A. That is what it means, that is what it meant, and I know of no other construction by common usage of the term other than what I have just stated.

Q. And that is before it is shipped away from treatment, which was outside of the realm of mining?

A. That is correct.

Mr. Casterlin: Now, we object to that as being leading and suggestive.

(Testimony of John Davis Bradley.)

The Court: Sustained, and the answer is ordered stricken.

Q. Where did mining stop, at what point did it stop, that is, that comes within the industry's understanding of the word 'produced,' where did it stop?

A. It stops at the point where you receive your returns from the products from the mine.

Q. Where does production from the mine stop, maybe I better put it that way, as distinguished from some further process of production? [156]

A. The product from the mine stops when the production process is complete so far as mining concentration terminology is concerned. It does not involve steps such as smelting that completely change the character and reduce the mined product to a metal.

The Court: Does mining itself, what constitutes mining, is that a term of any particular significance in the mining industry, as applied to different ores?

A. You have different mining methods, but mining is extraction.

The Court: For instance, you speak of mining gold ore, does that purport certain processes to a mining man, might not it be applicable to mining gold and cinnabar and tungsten?

A. No, sir, when you say mining, I don't think that you are describing the actual method of mining, but it describes the phase of the work being done, it is not sufficiently definitive to say what type of mining is being done but it does describe

(Testimony of John Davis Bradley.)

the extraction from the ground and any concentration.

The Court: That is what I was getting at. For instance,—of course, we are talking about the time of the contract,—if you said to a mining man at this time, that is, in 1941, we are mining cinnabar [157] or we are mining tungsten, what would that mean to a mining man, if you said we are mining tungsten up there, what would that mean to him that you were doing?

A. At that time a mining man would have thought that was pretty good.

The Court: That is not exactly what I am getting at, what if a man said "What are you doing there" and the answer was "we are mining gold ore", now, to a mining man, would that convey to him that you are doing certain things or were doing certain things up there at that mine? Everybody knows that mining means taking something out of the ground, that step is included in any definition of mining, I presume, but when you say to a mining man "we are mining quicksilver", does that convey to him that you are doing certain things?

A. Yes.

Q. Besides taking something out of the ground?

A. Yes.

The Court: What does it mean?

A. When you say you are mining quicksilver, you couldn't be mining it successfully—

The Court: —Mr. Bradley, just tell us posi-

(Testimony of John Davis Bradley.)

tively, don't argue, tell us positively what it means. If you meet a miner on the street, or met a miner on the street in December, 1941, if you met him [158] on the streets of Boise and he said "What are you doing up there at Yellow Pine?" and you say "We are mining quicksilver right now", what does that mean to him that you are doing up there?

A. It means to him that you are mining and——

The Court: ——That you are taking something out of the ground?

A. Yes, and recovering the quicksilver. By recovering I mean roasting.

The Court: That you are digging ore out of the ground and what else?

A. It means that you are roasting and condensing the quicksilver.

The Court: Anything else?

A. Marketing it.

The Court: Marketing what?

A. The quicksilver, the finished product.

The Court: And that is what mining quicksilver would mean to him there. All right, now then, if you said we are mining gold up there, what would that mean?

A. Well, I think you would usually describe each one. If you say "We have a gold mine", then he would probably say "At what rate are you mining" or "how are you mining".

The Court: But that isn't what he asked, [159] he didn't ask how you were doing it, he simply said "what are you doing", he didn't say are you

(Testimony of John Davis Bradley.)

making money or getting rich, he said "what are you doing up there at that hole in the ground" and you would say "we are mining gold". Now then, what would that mean to another mining man, what would that mean in December of 1941 that you are or were doing. Would he have a mental picture of what your operation was?

A. I think you would have to qualify it.

The Court: What if you didn't tell him any more than that, would that have any special meaning to him?

A. It would mean, in the normal instance, that you were extracting ore and concentrating it.

The Court: And then what?

A. Well, cyaniding it.

The Court: Cyaniding it or otherwise concentrating it?

A. If it is sulfide you are concentrating it and shipping the concentrates.

The Court: Shipping it where?

A. To a smelter.

The Court: And having it smelted into metal?

A. That is right. [160]

The Court: And if you said that you were mining gold, would that connote something different to him than if you said you were mining quicksilver?

A. Because you would have a different process in concentrating gold, you could hardly have a clean highgrade gold so that it didn't need concentrating.

The Court: I am speaking of the ordinary ter-

(Testimony of John Davis Bradley.)

minology. I suppose that you could have a vein of free gold?

A. It has been done.

The Court: Yes, but you would probably tell him all about that, but if you said you were mining gold up there what would that mean to a mining man, what would it normally mean to a mining man, if it meant anything special.

A. I am afraid I am not getting the point there.

The Court: Well, let's go to something else. Suppose you said that you were mining tungsten up there, would that impart to him any mental picture, as a mining man, of what process you were going through if he knew mining?

A. It would depend on the mineral.

The Court: But you said tungsten.

A. No, I said it would depend on what mineral of tungsten, tungsten is the metal, the element.

The Court: I don't know enough about it to know what mineral you are talking about, if I were a mining man I might know. What would you tell him you were mining up here in the way of tungsten?

A. I might say we are mining tungsten, and he might say, what mineral are you mining and I would say scheelite.

The Court: Now we are probably where we should have been had I known enough to ask the question. If you said "well, we are mining scheelite", would that impart to a mining man a picture of a certain process, it would indicate that

(Testimony of John Davis Bradley.)

you were taking ore out of the ground, and anything else?

A. It would indicate to him that certainly that ore had to be concentrated or else it was sufficiently high grade that it would have to be shipped.

The Court: Then it would mean that you were taking ore out of the ground and either shipping it or,—what, where would you ship it?

A. If it were sufficiently high grade it would be equivalent to a concentrate.

The Court: And if it were not?

A. You would have to concentrate it.

The Court: And where would that occur?

A. At the property. [162]

The Court: And that is what it means?

A. Yes.

The Court: And if you were mining gold, and told him you were mining gold, it would mean to him that you were getting gold good enough to ship to the mint or——

A. ——Or we would have to concentrate it.

The Court: Concentrating it in some manner or shipping it to a smelter?

A. Yes, sir.

The Court: And if you told him you were mining quicksilver, it would mean to him that you were getting it pure enough to sell as it is produced out of the ground——

A. ——No, in that instance, in the case of quicksilver I know of no deposits where they don't have—in the instance of a small deposit—I know

(Testimony of John Davis Bradley.)

of no instance where they wouldn't have a retort right there, and in case of a larger one a reduction works.

The Court: And if you told him you were mining quicksilver he would understand it, I take it, that you were taking it out of the ground and applying heat or some process to it there at the mine?

A. That's right.

The Court: I have another question to ask. [163] At the time this 1941 agreement was being formed was there any discussion by you with anyone representing the plaintiff, with respect to the tax question involved, such as depletion?

A. Yes.

Q. With whom was that discussed?

A. I think Mr. Worthwine discussed it, probably through me, with our tax attorney in San Francisco. I don't remember discussing it directly with Mr. Oberbillig.

The Court: That is all I have to inquire of this witness.

Mr. Ray: You may cross examine.

Cross Examination

Q. (By Mr. Casterlin): Mr. Bradley, you have testified concerning minerals. Now, tell us everything that has been produced out of that mine during the time you have had it.

A. Gold, antimony, tungsten, some quicksilver from the adjoining property which we originally had and then subsequently did not have.

(Testimony of John Davis Bradley.)

Q. Is that everything that has been produced out of those mines?

A. To the best of my recollection, that is correct.

Q. Did you mention antimony? A. Yes.

Q. Did you mention arsenic? [164] A. No.

Q. There was some arsenic produced?

A. Yes, but we didn't produce it in the common usage of the word, we were not aiming to produce arsenic, that was an impurity.

Q. Now, Mr. Bradley, if you meet a mining man or an ordinary prospector and, well, let's say you met a prospector and you asked him where his claim was located and he told you and you said "What are you producing up there?" would he name the minerals that he is producing?

A. Yes, I would expect him to.

Q. And if he had an antimony mine and you asked him what his mine was producing and he said antimony, you would understand it, wouldn't you? A. Yes.

Q. And he would understand you?

A. Well, I haven't said it.

Q. But you would understand each other if you talked to a prospector out here?

A. May I interject a point here?

Q. Yes.

A. That is, that silver should be added to the gold. Gold, silver, and antimony were the products.

Q. If you met a miner out here who was [165] going out to locate claims and you asked him where his claims were and he told you and you would

(Testimony of John Davis Bradley.)

say "What are you producing up there?", and if he told you that he was producing antimony, you would understand him, wouldn't you?

A. I would understand that he was producing antimony, but I would ask him how.

Q. You, you might ask him how, but if you said to him "What are you producing up there on that property" and he said "antimony", that would be an intelligible answer, wouldn't it?

A. Yes, in the common meaning, yes.

Q. And if he said he was producing gold, that would be intelligible?

A. In the common usage of the term you refer to the end metal although you are not producing the end metal.

Q. But you refer to the end product when you ask him what he is producing? A. Yes.

Q. And he might not have, as is the usual custom, any smelter on his property at all?

A. Very likely not.

The Court: The usual custom is not to have a smelter?

Mr. Casterlin: Yes, we will stipulate to that.

A. I might very well ask when he said antimony, what mineral, and how much, how are you doing.

Q. And by minerals you would understand that that included everything in the mineral family, wouldn't it?

A. No, I wouldn't understand that, it would include just that mineral that he said.

(Testimony of John Davis Bradley.)

Q. When you would ask him what mineral you are producing?

A. No, I would say, "How does your antimony occur, in what minerals?"

Q. You might ask him that?

A. Yes, I think I would.

Q. Yes, but you would know that the mine was producing antimony when he said "That is what I am producing up there", you would understand that, wouldn't you?

A. No, I wouldn't understand completely whether he was producing antimony as ore or in concentrates.

Q. But you would understand that antimony was coming from the mine?

A. I would understand it was antimony, as we used it, although it might be the mineral stibnite that was being concentrated, that was the product that was receiving attention, yes.

The Court: Before you leave that, are you leaving that now, Mr. Casterlin?

Mr. Casterlin: Yes. [167]

The Court: What would it mean to you, you said that you would understand what he meant, what would you understand?

A. That the man told me that he was producing antimony.

The Court: That he was mining antimony, what would that import to you?

A. That he had an antimony property that was worth mining.

(Testimony of John Davis Bradley.)

The Court: Of course, it would mean that he was taking something out of the ground, would it import anything more than that?

A. If he was doing it on a large enough scale it would mean either that he had a high enough grade of ore or he had a concentrator on it.

The Court: A concentrator on the property?

A. Yes, if it was a large enough property and sufficiently low grade.

The Court: Or it might mean that he was shipping?

A. Yes, or he wouldn't be mining it very long.

The Court: Shipping it where, I mean to what kind of concern?

A. To a smelter.

Q. This is probably repetition, Mr. Bradley, but when did you say that Mr. Worthwine became connected with your company as its attorney? [168]

A. I didn't say specifically, but I think that he did special work for us, perhaps prior to 1941, but I said that he became recognized during the war years as our local counsel, particularly when Mr. Davis became involved in World War II.

Q. That would be prior to the erection of the Yellow Pine smelter?

A. That he was doing specific selected work for us, yes.

Q. Was he your attorney at the time the Yellow Pine smelter was put into operation?

A. He was acting on our behalf, yes.

Q. Can you pinpoint about when he became your

(Testimony of John Davis Bradley.)

representative or attorney with respect to this Stibnite property?

A. He became classified as local counsel but still subject, whenever convenient to working with John Davis by correspondence, perhaps in 1942. But I don't remember exactly.

Q. Now, Mr. Bradley, about the time that you started building the Yellow Pine smelter, did you have any conversation with Mr. Oberbillig concerning an amendment to this 1941 contract?

A. Yes.

Q. And was the 1941 contract ever amended as a result of that negotiation? A. No.

Q. Now, that negotiation arose, did it not, over an argument concerning how you were to pay [169] royalty at the Yellow Pine smelter, isn't that true?

A. I wouldn't say that was exactly true, Mr. Casterlin, what I was striving to do in that instance was to arrive at some simple form that would preclude arguing. We had had a number of arguments in the past, and I felt that establishing a simple form rather than agreeing to smelter deductions as such, and having those up as a cause of complaint, that a simple form should be agreed to.

The Court: By a form what do you mean, a formula?

A. Yes, a formula, I would say a formula.

Q. Your minds never came to a meeting, you with Mr. Oberbillig on that point of a special formula, did it? A. No.

(Testimony of John Davis Bradley.)

Q. So that this dispute which arose, or the argument which arose, before the Yellow Pine smelter was put in operation had to do with how you would account for the royalties from the Yellow Pine smelter, that is correct, isn't it?

A. It is incorrect from this standpoint, that there was never a dispute at that point. I was endeavoring to illustrate to Mr. Oberbillig a simple way of accounting for our smelter charges, and the fact that it was never accepted, it was never in what you call a dispute. My correspondence, which I think was the main way, completely the way, of conveying my ideas to Mr. Oberbillig, was [170] only in one instance answered and then never to the point. It never became an argument.

Q. There was a discussion between you and Mr. Oberbillig, let us put it that way, concerning the amendment to the 1941 contract?

A. No, it was one-sided. I was endeavoring to get Mr. Oberbillig to understand what I was trying to do and I don't think that I ever got my point across, I never received——

Mr. Brown: ——We object to that, your Honor, as improper cross examination. It doesn't go to any issue in this case and we did not question the witness in regard to that on the direct examination.

The Court: What is the purpose of this, Mr. Casterlin?

Mr. Casterlin: The purpose is this, the defendant has endeavored to show, by long questioning, that Mr. Oberbillig, representing the United Mer-

(Testimony of John Davis Bradley.)

cury, agreed to accept these settlements and accepted these settlement sheets without any question.

The Court: The objection is overruled.

Q. Now, your suggestion to Mr. Oberbillig was, as I understand it, that the contract of 1941 should be amended so as to provide some particular formula for determining the royalties to be paid upon the product of the Yellow Pine smelter? [171]

A. It was simpler than a formula. What we did was to suggest that in lieu of 5% that the royalty on smelted products be 2.75%, which was more than necessary, but we were leaning over backward on the end product of the smelter so as to preclude the necessity of constant haggling on what were properly chargeable and accountable smelting costs.

Q. And that formula, you determined, should be applied to the Yellow Pine smelter?

A. Correct.

Q. And Mr. Oberbillig never did come to any agreement with you on that, did he?

A. No, he never agreed to that.

Q. So that this misunderstanding, if we put it that way, which started prior to the construction of the Yellow Pine smelter, continued on through, and you had suggestions one way or the other?

A. No, that is incorrect. We offered in lieu thereof, the best terms of all of the contracts that we had ever shipped under as a guiding light, for that to run for a period of three years, at which time we had tested that procedure by making ship-

(Testimony of John Davis Bradley.)

ments to other smelters and to have a review. Now, somehow or rather, I was led to believe,—let me say, somehow I was of the opinion, I guess that isn't any different either, is it? Anyway, I [172] assumed that Mr. Oberbillig had acquiesced because I had no written argumentative proposal to that particular proposition that I recall.

Q. So that any of these suggestions that you made were never accepted by Mr. Oberbillig, were they? A. I don't recall.

Q. Can you tell me, without any explanation?

A. No, never accepted except by never being rejected.

Q. Not being rejected? A. Yes.

Q. And that is your personal opinion, isn't it?

A. I do know that that 2.75 reduction offended Mr. Oberbillig and therefore was rejected. I don't know that the other was rejected, and I didn't know at that time.

Q. Was it ever accepted?

A. Yes, in some period of time.

Q. Where did Mr. Oberbillig accept your suggested changes?

A. As evidenced by accepting the returns.

Q. Where did Mr. Oberbillig, or anyone in his behalf, tell you that your offer to reduce the 5% to 2.75% was accepted?

A. I just finished saying, Mr. Casterlin, that he did reject that, but he did not reject the other nor did he formally accept the other.

Q. He neither accepted nor rejected?

(Testimony of John Davis Bradley.)

A. But he did reject the 2.75, therefore, I felt [173] that the other was accepted and satisfactory.

Q. That was your interpretation of it?

A. Yes sir.

Q. And the result of your interpretation would be for your benefit, wouldn't it?

A. No, for Mr. Oberbillig's benefit.

Q. Weren't you trying, Mr. Bradley, to get some particular formula for the Yellow Pine smelter which would preclude Mr. Oberbillig's company from receiving 5% of the money that you received from the end product?

A. That never occurred to me.

Q. It never occurred to you?

A. No, all I was striving for was a simple way of arriving at the net smelter returns to our own smelter, so that there would be no room for argument.

Q. And this simple proposition that you made would allow you to deduct all the expenses of smelting, wouldn't it?

A. It should have, certainly.

Q. I am not asking you that, it would allow you to deduct all of the cost of smelting?

A. No, it would not have. The 2.75 was definitely in the United Mercury Mine's favor, and we proved that. Of all of the charges of smelting we would have borne more than our share so far as the royalty is concerned.

Q. Let's put it this way, Mr. Bradley, if you [174] had paid the United Mercury royalty on all

(Testimony of John Davis Bradley.)

of the money that you received from the end product from the Yellow Pine smelter the United would have received more money *that* you have paid them under your own formula, wouldn't they?

Mr. Ray: I think that was stipulated.

Q. I don't think so.

The Court: What do you mean by your own formula, the accepted formula?

Mr. Casterlin: The accepted formula, yes.

The Court: Do you mean, Mr. Casterlin, that the defendant, if they had not charged for smelting and had given a 5% royalty on whatever it received for the end product after smelting, that it would have paid more money to the Plaintiff than the 2.75, was that the figure?

A. 2.75, yes, which wasn't the formula used.

Mr. Casterlin: Yes, your Honor, that is what I mean.

A. May I repeat my answer because it needs qualification.

The Court: Yes, you may.

A. I said that I didn't think, however, I would have to check the record, and the reason for that is that much of the product that was produced at the smelter is still unsold. [175]

Q. I hand you what purports to be a letter under date of April 14, 1948, from you, John D. Bradley, the Executive Vice President, to John J. Oberbillig, President, which has been marked for identification as Exhibit 11.

The Court: This is Exhibit 11 for identification,

(Testimony of John Davis Bradley.)

is it not? According to my notes it is attached to the Oberbillig deposition, a copy, that is. Now, what you produce here is the original, it appears to be the original.

Mr. Casterlin: That's right, we will put that in, we will offer that as Exhibit Number 11.

The Court: What you are offering now appears as the original of the copy marked Exhibit 11 and attached to Mr. Oberbillig's deposition.

Mr. Casterlin: Yes.

The Court: Do you wish it marked as Exhibit 11?

Mr. Casterlin: Yes.

The Court: The clerk will so mark it and hand it to the witness.

Q. Mr. Bradley, I will ask you if that is your signature attached to that letter?

A. Yes, it is.

Mr. Casterlin: We now offer Exhibit Number 11.

The Court: Is there any objection? [176]

Mr. Ray: For what purpose is that offered?

Mr. Casterlin: For all purposes.

Mr. Brown: I think we have no objection except that we reserve the objection that it is not proper cross examination.

The Court: The objection is overruled and it is received in evidence as Exhibit 11.

[See pages 382-387.]

Q. I hand you, Mr. Witness, a letter dated December 2, 1948, purporting to be a letter from John D. Bradley, Executive Vice President, to Mr. J. J.

(Testimony of John Davis Bradley.)

Oberbillig, President, and it is marked for identification as Exhibit Number 31.

The Court: Has that been marked as Exhibit 31?

Mr. Casterlin: I have asked the Clerk to mark it.

Q. I ask you to state if that is your name attached to that exhibit? A. Yes, it is.

Mr. Casterlin: I now offer Exhibit Number 31.

Mr. Brown: We have no objection except that we have the reservation that it is improper cross examination.

The Court: The objection is overruled and [177] it is received in evidence as Exhibit Number 31.

[See pages 436-440.]

Q. Mr. Witness, I hand you what has been marked as Exhibit Number 29, and admitted in evidence. Calling your attention to the second page of that exhibit and the first line "gross sales value per attached invoice, \$34,228.93", that item has reference to Page One of that exhibit? A. Yes.

Q. Now, the second line, "less operating costs applicable, including depreciation, \$6,295.25". Was that the only report that you made to the United as to what constituted those deductions?

A. Yes, I believe that was all that was sent to the United describing the deductions.

Q. On Page Three?

A. I don't have a Page Three, Mr. Casterlin.

Q. Calling you attention to the contract of 1950, which is set forth at Page 59 of the transcript,—Page 69, pardon me, Mr. Bradley. The last paragraph which is Number 3, "Save and except for

(Testimony of John Davis Bradley.)

the above and foregoing postponement of royalties, the said conveyance and royalty agreement, in all its particulars and provisions shall remain in full force and effect." Would you say that the purpose of this 1950 contract was for the purpose expressed in it or for some other purpose?

A. The purpose, I have forgotten what is [178] expressed in it, but the purpose was to postpone the royalties for that period.

Q. And in other respects the original contract would not be amended or changed at all?

A. That's right.

Q. Calling your attention to Exhibit 5A,—strike that question, please,—calling your attention to the original contract, which is Exhibit Number 7, and which appears in the transcript at Page 17 and reads as follows: "By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals, or values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho." Will you tell us who first proposed that language, whether it was you or Mr. Oberbillig?

A. I believe I did.

Q. So that definition came into the 1941 contract as it was proposed by you?

A. It was retained as proposed by me in the 1939 contract, and retained in the 1941 contract for obvious reasons.

Q. This probably is repetition. The Yellow Pine

(Testimony of John Davis Bradley.)

smelter was built by Bradley's as an economic movement, was it not?

A. It proved to be a very uneconomic movement.

Q. My question is, Mr. Bradley, the Yellow Pine smelter was [179] built by Bradley's as an economic project?

A. Yes, that was the intent at the time.

The Court: And that would mean to try and make more money.

Q. By that economic project you endeavored to get larger returns from your operation than you would have otherwise?

A. We endeavored to get some, we could see that with the grade of the ore we couldn't—

Mr. Casterlin: —That answers the question, Mr. Bradley.

The Court: That is what they are in business for.

Mr. Casterlin: That was the purpose of my question.

The Court: Whenever a company stops trying to make money for its stockholders then, of course, the one in charge doesn't stay there very long.

Mr. Ray: I think, your Honor, that the witness started to explain his answer and we would like that in the record.

The Court: Unless the answer requires some explanation, and I don't see that it was, he wasn't asked the purpose in so many words.

Q. The United never had anything to say with

(Testimony of John Davis Bradley.)

respect to directing the operations at the mine, did it? [180]

A. It did in the early years but never once,—and that was one of the reasons that we switched to the gross royalty.

Q. Under the terms of the original contract you owned the mine?

A. Under the terms of the '41 contract.

Q. Yes?

A. You are referring now from then forward?

Q. Yes?

A. Yes, they had no right to interfere with the operation of the mine according to the terms of the contract of the sale.

Mr. Casterlin: That's all.

Redirect Examination

Mr. Ray: Before I interrogate the witness, I should like to ask counsel to produce the original of the letter dated March 31, 1948, which is referred to in Exhibit 11.

Mr. Casterlin: I think we will save a little time, if the Court please, if we may have a little time.

The Court: Very well, just go ahead.

Mr. Ray: I am sorry, your Honor, but I can't very well conduct my re-examination on these [181] letters very well until we have the other.

The Court: Now, the Exhibit is marked for identification as Defendant's Exhibit Number 32.

The Clerk: That is right.

Q. Now, Mr. Bradley, I understand you have

(Testimony of John Davis Bradley.)

in your possession a document which is marked as Defendant's Exhibit 32. Will you state what it is.

A. It is a letter from me.

Q. Signed by you? A. Yes.

Q. And addressed to whom?

A. To Mr. Oberbillig, President, United Mercury Mines Company.

The Court: Was that letter produced from the files of the plaintiff?

Mr. Ray: Just produced from the files of the plaintiff.

Q. Now, will you refer to Exhibit Number 11, and near the bottom of the page, in reference to a letter of March 31, do you see that?

A. Yes, I do.

Q. Can you state whether Exhibit 32 is the letter referred to in Exhibit 11? A. Yes. [182]

Q. Mr. Bradley, you have been interrogated on cross examination, with respect to a proposal which involved the figure 2.75, do you remember that?

A. Yes.

Q. And do you have in mind also that the royalty figure in Exhibit 7 is 5%? A. Yes.

Q. And you submitted the figure 2.75 to Mr. Oberbillig, did you not? A. Yes, I did.

Q. And he thought, as he told you, that was a reduction of the 5% royalty? A. Yes, he did.

Mr. Casterlin: Just a moment. I don't like to object to the question as leading and suggestive, but I do think the witness should testify.

Q. What was your purpose in preparing—

(Testimony of John Davis Bradley.)

The Court: —The objection to that last question is overruled and the answer may stand.

Mr. Ray: May I withdraw that portion of the question I just started?

The Court: You may.

Q. What did you intend the 2.75 to mean?

A. I meant——

Mr. Casterlin: —I object to that at this [183] time as calling for an interpretation, apparently, of an Exhibit which has not been admitted in evidence.

Mr. Ray: You asked, Mr. Casterlin, if he wasn't trying to get the royalty amended or reduced.

Mr. Casterlin: If that is the question, I have no objection to it.

Mr. Ray: And by the way, I would like to offer Exhibit Number 32 at this time.

The Court: Is there any objection?

Mr. Casterlin: No objection.

The Court: It will be admitted.

[See pages 440-446.]

Mr. Ray: Except as to the question asked on cross examination which went to Mr. Bradley's purpose and motive, I would simply read the letter to show what they are and were, but since the motive was gone into and inquired about on cross examination I want to ask what the purpose was in proposing this 2.75?

A. My purpose in proposing that——

The Court: —Was that a question, Mr. Ray?

Mr. Ray: If I may have that as a question.

(Testimony of John Davis Bradley.)

A. My purpose in proposing that was for that royalty rate to be in lieu of the 5%, and then——

Q. 5% of what? [184]

A. 5% on the net smelter returns, in which case we felt that we might be involved or that it might become a difficult point in explaining to United Mercury what the smelting charges were. So, in lieu thereof, and in order to simplify the accountability of the royalty I proposed 2.75, which was far and away ahead of the 5% of the net smelter.

Q. Let me see if I can get at it this way,—you construed 5% as the net royalty applicable to net smelter returns? A. Yes.

Q. Were you now looking for a percentage which would yield equivalent or approximately the same if applied to the end product of the smelter?

A. That is correct, and as I have tried to point out, and pointed out in those letters, it was on the United Mercury's side of the ledger so far as favorability was concerned.

Q. Why is that?

A. Now I wonder. I was trying to be overly fair.

Q. In other words, was it your opinion that 2.75% on the products after they had gone through the smelter would be more than 5% on the net smelter returns?

A. Yes, and that can be more than confirmed by checking the record.

Q. Mr. Bradley, you were asked who first proposed the introduction into this agreement of the

(Testimony of John Davis Bradley.)

net revenue provision, and you stated that you did, to whom did you propose it?

A. To Mr. Worthwine. [185]

Q. Where and when?

A. In his office in Boise at the time, during the period of negotiation of the 1939 contract.

Q. Explain to the Court what occurred at that time in that conference between you and Mr. Worthwine, when you first proposed the inclusion of the net revenue clause into the agreement?

Mr. Casterlin: We object to this until it is determined in what capacity Mr. Worthwine was acting, because it appears now that Mr. Worthwine was representing Mr. Oberbillig, and also it appears that Mr. Worthwine was representing, in special matters, Bradley, at the time of the '41 contract.

Mr. Ray: I would like to ask counsel if there is any dispute that Mr. Worthwine was representing the Plaintiff in the negotiations of the 1939 contract or the 1941 or the 1950? I would like to ask if there is any dispute about that?

Mr. Casterlin: There is a dispute with reference to the '41 contract, because the testimony here is that——

The Court: ——The question deals with the 1939 contract. The objection is overruled. He may answer the question.

Q. Who was Mr. Worthwine representing?

The Court: There was a question unanswered.

A. Yes, there was a pending question.

(Testimony of John Davis Bradley.)

Q. I thought it was answered,—go ahead, Mr. Bradley.

A. The reason being that we had other mineral products that were not covered by net mint and net smelter clauses. Mr. Worthwine, presumably after consultation with Mr. Oberbillig, presented net milling returns——

Mr. Casterlin: ——I want to object——

Mr. Ray: Let's strike out the word "presumably". You assumed that, did you, Mr. Bradley?

A. I was presented this draft by Mr. Worthwine.

The Court: By this draft, you refer to what?

A. Exhibit 5A, which showed in addition to net mint and net smelter, a clause to cover the other mineral products of which we had evidence and possible indications as to the future. Mr. Worthwine phrased it under the caption "net milling", which to me was not as broad as "net revenue", owing to the reason that the word milling, for example, would perhaps not cover the actual mercury processing. You might have high grade ore that wouldn't be milled.

Q. No, just a minute,—have you encountered mercury in its free state? [187]

A. Yes, I have.

Q. And when encountered in its free state is it sold directly as it is taken from the earth?

A. If it can be captured.

Q. Go ahead.

A. That concludes my reply.

(Testimony of John Davis Bradley.)

Q. Did you have before you at that time for that discussion, the document that has been identified as Exhibit 5A? A. Yes, I did.

Q. Did you at that time make the notations in your handwriting that you have heretofore discussed?

A. I made a number of notations——

Mr. Casterlin: ——We object to that as being incompetent, irrelevant and immaterial in view of the witness' testimony.

Mr. Ray: I will re-offer Exhibit 5A.

The Court: But your question is hardly intelligible considered in the light of the fact that the other evidence is at present excluded from the record.

Mr. Ray: That's right, I should keep that in mind. I am now, your Honor, re-offering Exhibit 5A.

The Court: I suggest that you reframe the pending question. [188]

Mr. Ray: I will withdraw that question.

Q. At the time you had this discussion with Mr. Worthwine and at the time that the net revenue clause was first proposed, did you have before you a draft of the contract submitted to you by Mr. Worthwine?

Mr. Casterlin: We object to that until we know what contract he has in mind that was submitted to him.

Q. Did you have a preliminary draft of the '39 contract?

(Testimony of John Davis Bradley.)

which states the net revenue clause and the word [191] "normal" as a limitation upon the smelter deduction?

A. Only the added words under net smelter returns, and certain minor corrections.

Mr. Ray: I think Mr. Casterlin stipulated that at the time this contract was negotiated Mr. Worthwine was representing the Plaintiff.

The Court: You mean the 1939 contract?

Mr. Ray: Yes.

Mr. Casterlin: The 1939, yes, but this amendment is for use in the '41 contract.

Q. Mr. Bradley, you also negotiated the 1941 contract with Mr. Worthwine, didn't you?

A. Yes.

Q. Who was he representing in that negotiation?

A. The United Mercury Mines Company.

Q. Who represented the Bradley Mining Company? A. John Parks Davis.

Q. Were you in the negotiations?

A. Yes, I did the negotiating and so far as the legal side of it was concerned I submitted it to Mr. Davis for his approval.

Q. Mr. Worthwine was not representing you in those negotiations? A. No. [192]

Mr. Ray: I don't think we have anything further with this witness.

The Court: We will start with the Recross at two o'clock.

(Testimony of John Davis Bradley.)

March 20, 1957

2:00 O'Clock P.M.

The Court: You may proceed.

Mr. Casterlin: No Recross.

Mr. Ray: At this time, if the Court please, we ask the Court for an Order making a part of the evidence the testimony which went in as excluded evidence, the testimony which went in in connection with Exhibit 5A.

Mr. Casterlin: We object to that on the ground that all of the evidence is not competent, relevant, or material in view of the limitation of the cross examination of this defendant on particular matters.

The Court: The objection is sustained. The motion places such a burden on the Court to remember everything that was asked of and answered by the defendant concerning Exhibit 5A under the evidence which was excluded. It seems to me that you would have a better record if you proceed to ask the questions which you think you would like to have answered. [193]

Q. (By Mr. Ray): At the time, Mr. Bradley, that you and Mr. Worthwine discussed the deletion of the milling clause and the substitution of the net revenue clause, did you explain to Mr. Worthwine why you suggested the substitution for the milling clause, and what material the net revenue clause might relate to?

Mr. Casterlin: To which we object on the ground that Mr. Worthwine is a third party to the con-

(Testimony of John Davis Bradley.)

tract and he might have been acting with respect to his own interest and not with respect to the interest of the United Mercury, and further that it is incompetent and irrelevant to any of the issues in this case, and invades the province of the Court in view of the fact that it is a self-serving declaration and not a meeting of the minds of the parties.

Mr. Ray: I want to point out that Mr. Worthwine was not a participating party to the contract.

The Court: I don't have any problem with the fact that he was representing, in addition to himself, at that time——

Mr. Ray: ——He wasn't representing himself at that time.

The Court: He had an interest in the contract [194] no doubt, but the problem that I have is whether or not that portion was opened up by the cross examination.

Mr. Ray: He was asked if he proposed the introduction of that contract,—that clause, and he said he did, and I am asking, at the time he introduced it, what was said.

Mr. Casterlin: The question, I think, was who first proposed the definition of the net revenue clause.

The Court: I believe the purpose in asking that was to show that the authorship was in the defendant and therefore, you would argue, that the clause must be construed most strongly——

(Testimony of John Davis Bradley.)

Mr. Casterlin: —That's correct, that was the purpose of it.

The Court: Here we cut across much of the negotiation problem,—the negotiations were merged in the written document, the language is there, and the whole issue here is, what is the content of the language? What is the purpose of this?

Mr. Ray: The purpose is that we want to take ourselves back and put ourselves in the surroundings under which the defendant introduced that, and we think we are entitled to show the circumstances under which it was introduced. He [195] suggested the substitution of one provision for another.

The Court: Yes.

Mr. Ray: Why did he do it?

Mr. Casterlin: We take the position that it is immaterial why he did it until it is shown that there is some uncertainty or ambiguity in the language or that it has a peculiar meaning which was not understood, in the ordinary sense of the words, by the parties to the contract.

The Court: I will sustain the objection. If it is not in the record of excluded evidence, you may place it there. Are you content that the answer called for by the last question is in the record of excluded evidence?

Mr. Ray: Yes.

Mr. Brown: If your Honor please, yesterday the defendant tendered the Pretrial Conference

(Testimony of John Davis Bradley.)

Order in evidence. We do not have the number of the exhibit.

The Court: Exhibit 30, according to my notes.

Mr. Brown: However, the Exhibit contains a number of stipulations which at the moment, on the basis of the Order itself, the Plaintiff has reserved objection to certain of the stipulations and [196] then reserves one specific objection on the ground of relevancy and materiality—

The Court: I understand those objections were not urged when the document was offered.

Mr. Brown: We understand that too, but we are wondering whether we were in rather a blind alley so far whether they were overruled or whether the stipulations stand actually as admitted.

The Court: The objections were reserved and were not urged at the trial, that is the way the record stands now as I understand it.

Mr. Brown: We just wanted to be sure of that.

The Court: Is that your understanding, Mr. Casterlin?

Mr. Casterlin: Yes, they were reserved.

The Court: And were not again urged when the document was offered?

Mr. Casterlin: They are still reserved.

The Court: Very well, if you feel they are still reserved, they are overruled.

Mr. Ray: We have no further questions of Mr. Bradley. [197]

Mr. Casterlin: No further questions.

Mr. Ray: We have no further witnesses.

The Court: Does the Defendant rest?

Mr. Ray: The Defendant rests.

The Court: Any rebuttal?

Mr. Casterlin: None, the Plaintiff rests.

The Court: Would you gentlemen like to take up oral arguments this afternoon?

(Remarks of Court and Counsel concerning time of arguments not transcribed.)

Mr. Casterlin: May I inquire as to whether there will be briefs after the oral argument?

The Court: Well, I hope not, I hope it will not be necessary to have briefs, if I can be clear enough that will not be necessary. I presume that this litigation isn't getting any better with age. I propose, if I am clear enough on the matter, I will decide it at the conclusion of your oral argument. As I see it now, if the Defendant is entitled to deduct the smelting charge as to the matter in controversy, then the Judgment should go to the Defendant. If the Defendant is not entitled [198] to recover the smelting charges, then Judgment should go to the Plaintiff. I don't know how much is at stake here, probably a great deal, but that is immaterial.

Mr. Casterlin: That is just what I had in mind and was hoping would result from our little conversation, that the Court would indicate the points that he would like to hear us on.

The Court: Are you agreed that is the situation, fairly stated, that is, if the smelting charges are

properly deducted then Judgment must go to the Defendant, and if they are not properly deducted then Judgment should go to the Plaintiff?

Mr. Casterlin: In other words, if the net smelter return provision applies then Judgment is for the Defendant.

The Court: By that you mean if the net smelter returns provision applies to the ores smelted at the Yellow Pine?

Mr. Casterlin: Yes.

The Court: Then Judgment would go to the Plaintiff.

Mr. Ray: To the Defendant.

The Court: That's right, I am sorry. [199]

Mr. Casterlin: And if the net revenue provision applies then Judgment goes to the Plaintiff with the provision for accounting.

The Court: Yes, an accounting would be necessary I presume.

Mr. Casterlin: That simmers it down pretty well, and I think with that limitation we surely can get through in an hour on a side.

The Court: You may take whatever time you feel is necessary, say, up to an hour and a half on a side.

You don't know, I presume, what is in controversy. It is more than the question of smelter charges.

Mr. Casterlin: Yes.

The Court: What is in controversy is whatever the defendant may receive upon the royalty——

Mr. Casterlin: —If the net revenue clause prevails we are not interested in smelter charges.

The Court: You are only interested in the returns that the Defendant receives.

Mr. Casterlin: If the net smelter returns provision applies we are still not interested in an accounting, because it is admitted that they have [200] properly accounted for everything under their theory of the net smelter returns.

The Court: An accounting would be necessary to know what is at stake then?

Mr. Ray: There is an Exhibit in the files somewhere, I have forgotten now just where it is, where in response to an interrogatory there is a tabulation showing what we sold, what the products were that were sold, and what we received for them.

Mr. Casterlin: And on which the 5% was not paid.

Mr. Ray: That is right.

The Court: I don't need to say to you gentlemen, able lawyers that you are, you know what the amount is which is involved here, and someone is going to be hurt by this Judgment tomorrow, if I am able to render a Judgment tomorrow, and if you have any disposition to settle the matter, probably this is the last chance. Is there anything further, gentlemen?

Mr. Casterlin: Nothing from us.

Mr. Ray: Nothing further.

The Court: Then Court will be adjourned until tomorrow morning at 10:00 o'clock. [201]

March 21, 1957

10:00 O'Clock A.M.

(Arguments of Counsel.) [202]

* * * * *

The Court: The contract is admitted and the salient features that we are involved with are, of course, as set forth on pages 15 to 18 of the record on appeal, which is excerpted from Exhibit Seven here.

We bear in mind that the contract was made in 1941 and the smelter built in 1949. Our problem here is to ascertain the intention of the parties as manifested by the writing when read in the light of the facts and circumstances in evidence surrounding execution. The controversy arises, of course, because the contract is unclear as applies to this subsequently constructed smelter operation on the property, although admittedly the contract contemplated the possibility. It did not literally in so many words cover the contingency of the smelter on the property owned and operated by one of the parties to the contract.

It is stipulated, of course, at Q on Page six of the Pretrial Conference Order: "That, if under the terms of the contract, defendant, Bradley Mining [203] Company, is entitled to make any charge or deduction for smelting ores in the Yellow Pine Smelter, the charges and deductions so made by Bradley Mining Company have been proper charges and deductions, and all settlements made with the plaintiff have been correct."

“If it is ultimately determined that the net smelter returns provisions of the agreement is applicable to the operations of the Yellow Pine Smelter for ores, concentrates, metals and values taken from the claims described in the agreement, then the settlement made by Bradley have been correct as to the minerals, ores, metals and value processed at the smelter.”

“That there is no dispute as to the meaning and interpretation of the net mint return clause of the contract.” That appears under R, at the top of page seven of the Pretrial Conference Order.

I find that this contract was made by experienced mining people, including the principal draftsman,—I say principal, at least it appears in the record to be a fair inference that Mr. Worthwine was the principal draftsman, and a party interested in the contract, and the performance of it as it turned out, so I find that the parties contracted with reference to the practices and customs in the mining [204] industry prevailing at that time and as they envisioned such might be over the years. I think one significant fact that we may be inclined to forget at times, and one that should be kept constantly in mind, these parties envisioned this arrangement to last for ten centuries. That is a bold undertaking. I would hate to be called upon to envision what may be going on in the mining industry in the year 2000, much less the year 2900 and something, nine centuries later, but it is admitted under S, at Page seven of the Pretrial Conference Order: “That before 1939 and thereafter at all times material to this

action, it was the practice and custom in the smelting industry for companies who own and operate smelters to also own and operate mines; that it was likewise the practice and custom in the industry for companies owning mines and also mining smelters to ship their mine produce to their own smelters; that it was likewise the practice and custom with respect to owners of smelters and mines, to also lease mining properties from other independent owners, and send the produce extracted therefrom to their own smelters and to settle for the product so shipped on the same basis as such smelting companies would settle with independent or custom shippers; that it was a practice [205] and custom of the trade that where the ores treated came from mines owned by the owners of smelters, or came from mines leased and mined by the smelter owner or came from independent custom shippers, that the smelting charge and the cost of transportation of concentrates to the smelter were deducted to arrive at a net amount commonly referred to in the mining and smelting industries as net smelter returns."

Under T on Page seven it is stipulated: "That it is a matter of common knowledge and historically recognized in the mining industry that the milling of ores to reduce such ores to a concentrate form is a part of the mining process, and that the smelting of ores is not a part of the mining process."

There has been evidence of other customs and practices in the mining industry, that evidence stands uncontradicted. The other surrounding facts and circumstances siding in the interpretation are

the 1939 agreement, Exhibit 5, and the provisions of that agreement, and it is uncontradicted that one of the purposes of the 1941 agreement was to reduce the amount of royalty required to be paid by the defendant, and, as it has been developed here in our discussions today, the defendant's purpose to get a reduction in royalty, for obvious economic reasons [206] the plaintiff was moved to grant it because the plaintiff's purpose thereby was to induce defendant to a more intensive mining of the ores, particularly the low-grade ores on the property, or which might thereafter be found on the property. Having in mind again that this five percent arrangement was to last for a thousand years and even longer if paying values were found. As I have said before, it is uncontradicted that the possibility that the defendant might build a smelter at the site of the mine was discussed during the negotiations of the 1941 contract, and it is admitted under P of the Pretrial Conference Order at Page six: "That at the time of the execution of the contract, December 31, 1941, there were no smelters located at Cascade, Idaho." The contract itself, as was developed this morning envisages the possibility of a smelter near the mine and it was conceded in argument that that referred to the possibility that the defendant itself might build a smelter at or near the mining property. The provision in question appears at Page 18 of the Transcript of the record, and reads: "Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be de-

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ducted from the net smelter or reduction returns, a fair charge for trucking [207] from the mine to such smelter or reduction works.”

I have already referred to the custom and practice with respect to the operation of smelters. The parties contracted in the light of that practice. There is uncontradicted evidence that tax problems were discussed during the negotiation of the 1941 agreement, including the problem of depletion, and it seems a fair inference that the parties did contract with respect to these tax problems existing and possibly contemplated for the future end, of course, it will be assumed that they contracted with reference to existing laws. The Internal Revenue Code of 1939 at that time, specifically Section 114 (b) (4) (B) made provision for depletion allowances computed upon gross income from the property to mean the gross income from mining. The Statute defined the term “mining”, “to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied [208] thereto”, and then the statute proceeds and defines the ordinary treatment processes incident to mines, and states: “The term ‘ordinary treatment processes’, as used herein, shall include the following”,

in the case of many minerals, including gold and silver, "which are not customarily sold in the form of crude mineral products,—crushing, grinding and beneficiation by concentration, such as gravity, flotation, amalgamation, electrostatic, or magnetic, cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining)", and continuing "or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores." The statute thus attempts to define the ordinary treatment processes normally applied by mine owners in order to obtain a commercially marketable mineral product. Of course, when that product is obtained, that is the point at which the computation must begin for the purposes of depletion, or to put it another way, in computing the gross income from mining an operator may not proceed beyond these ordinary treatment processes, or he may not count the [209] income,—beyond the ordinary treatment processes normally applied in order to obtain a commercially marketable product. Thus, in the case of *Helvering v. The Bankline Oil Company*, 303 U.S., Page 262, that was a case in which the Court refused to allow the depletion based on the sale of the end product because that included some refining processes beyond the ordinary treatment processes normally applied.

In addition to the surrounding circumstances

there is certain conduct of the parties subsequent to the 1941 agreement, which throws light upon the intention of the parties, and that is this question of the tungsten ore, the uncontradicted evidence is that the tungsten ore was subjected to a flotation process at the mine, and it is interesting to note that the flotation process is included among the ordinary treatment processes by the mine owners in the statute that I just referred to of the Internal Revenue Code. These concentrates resulting were sold in the eastern market direct from the mine, reports were made, and royalty paid accordingly under the net revenue clause. Then there were certain tungsten concentrates that were sent to the defendant's Boise purification plant, and with respect to those, the net smelter return method of computing royalty was [210] used. Then there is the question of recitals in the 1950 modification agreement, Exhibit Number 6, which appears at Page 69 of the record transcript, in more particular the recitals with respect to May, 1950, royalty, which the uncontradicted evidence shows were computed according to the net smelter returns method.

I find that the parties, having in mind that this agreement was to last for such an unusually long period of time, that they envisioned, not only the possible method of marketing the mine product from the property, but also the possible variety of the minerals which possibly would be produced and marketed in the future, including gold, silver, antimony, tungsten, quicksilver and so forth, and as I read the provisions in question and particularly the

provision commencing at Page 15 of the Transcript of the record, Exhibit Number 7, the 1941 Agreement, we first find that there is a five percent royalty promise on all net smelter returns, net revenue, and net mint returns, as defined herein; and then over on Page 17 we find that net smelter returns are defined, net revenue is defined, and net mint returns defined. Then, reading on through the provision with respect to transportation, we find that the parties refer to the three methods, I shall call them, handling returns. Referring [211] to those methods as net smelter, market or mint returns. Smelter, market or mint,—net smelter, market and mint returns, smelter, market or mint, to which the same are trucked and so forth. The emphasis upon market is persuasive in the light of all of the other circumstances, that the parties have in mind here possible marketing methods, envisioning the possibility over the years, so they, as to anything marketable, in a condition to be marketed, the mint,—at the time they contracted the mint was the market. As to anything required to go to the smelter, the smelter was the market. As to other matters, as to concentrates, ores, metals or values, the net revenue provision was intended as a catch-all,—another method of marketing direct from the property. In other words, by transporting the product directly from the mine to the mint whenever the quality would permit such a relatively simple operation; by sending it to the smelter to be processed in the customary way, and in the third place, by marketing ore concentrates and values direct to third per-

sons from the mine, after the mining process had been completed. This evidence of custom and practice and other surrounding circumstances and subsequent conduct is not contradicted, nor is it otherwise illumined by any testimony from [212] either Mr. Worthwine or Mr. Oberbillig.

It is my view that the Plaintiff's construction would read the net smelter returns provision out of the contract, since the net revenue clause is general and covers everything not otherwise covered. If the net revenue clause is not the general catch-all then there is no explanation for having the mint and the smelter returns clauses in the contract, they are specific and appear to limit or control the general,—by the net revenue is meant the amount paid by the purchaser from the sale of concentrate, any purchaser. It is broad enough, as pointed out this morning, to cover whatever is covered by the net mint returns and whatever is covered by the net smelter returns. In any event, the plaintiff's construction would read out of the net smelter returns clause the phrase, it being understood that the smelter will deduct its normal smelting charge and charges for railroad, freight, and so forth,—it wouldn't read out the freight provision, of course, but it would read out the smelting charge provision, or it would necessarily read into the clause the words 'third-party owned smelter', or as has been said here, 'outside smelter', or something of like effect. If the smelter was not owned by one of the parties to the [213] contract then it had to be a third-party owned smelter.

At this juncture it might be helpful to observe again that it was agreed that the parties contemplated that the defendant might erect a smelter, and it is said, and I so find, that in that contemplation they inserted in the contract, and it appears on Page 10 of the Transcript record: "Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking" and so forth. One of the most compelling purposes or one of the most compelling considerations, as I find it in interpreting this contract, is the purpose the parties had in setting or putting aside this 1939 agreement, and creating the 1941 agreement. It is admitted that the purpose of the defendant, of course, was to get the lower royalties, but important here is the purpose of the plaintiff in granting the lower royalties, and that purpose was to induce and make it economically feasible and attractive for the defendant to mine ores of a lower quality. It's admitted here that the construction of this contract, which would not permit the defendant to deduct the smelting charges, would result in substantial increase in the [214] amount of the royalty over that that would be payable were the net smelter return provision to apply whenever ore is smelted. That in itself, as I view it and find, would be a construction contrary to the purpose of the contract and contrary to the plaintiff's own avowed purpose at the time the contract was executed.

Accordingly, I find that the plaintiff is entitled to a declaratory judgment, but not as prayed for.

The judgment will be, declaring and decreeing that the proper legal method for determining the amount of royalty due United from Bradley under the terms of the 1941 contract for the minerals, ores, metals and values extracted or produced from the mining claims described in the agreement and conveyed to Bradley and smelted at the Yellow Pine smelter, owned by Bradley, is by the use of the net smelter return provision as defined in the agreement. I am referring now to the interpretation of the prayer of the Complaint as set forth at the bottom of Page 1 and the top of Page 2 of the Pretrial Conference Order.

Plaintiff is entitled to a judgment declaring it is the duty, under the contract, of Bradley to furnish the United the amounts paid by purchasers from the sale of minerals, ores, metals and values [215] extracted from said mining claims, and smelted at the Yellow Pine smelter, and the marketing costs and shipping costs from Cascade, Idaho.

The Plaintiff is entitled to further declaration that under the provisions of the agreement,—appearing at the bottom of page 16 of the transcript, to which we have been referring here,—. It is the duty of Bradley to furnish United all necessary information that United may require to assure it that it is receiving the royalty to which it is entitled under the terms of the agreement, and, of course, the right to inspect, examine, and make copies of the books and records of Bradley and sup-

porting data at least every six months, so as to enable United to satisfy itself that it is receiving its proper royalties.

There is no necessity under this view of the agreement to require an accounting and that will not be required.

The Court will rule that each party bears its own costs, and the Findings of Fact and Conclusions of Law and Declaratory Judgment will be prepared by counsel for the defendant. [216]

* * * * *

[Endorsed]: Filed July 16, 1957.

DEFENDANT'S EXHIBIT No. 4

[Rejected]

AGREEMENT

This Agreement, Made and entered into this 3rd day of October, 1930, by and between the United Mercury Mines Company, a corporation organized and existing under and by virtue of the laws of the State of Idaho, as party of the first part, and the Yellow Pine Company, a corporation organized and existing under and by virtue of the laws of the State of California and authorized to do business in the State of Idaho, as party of the second part, Witnesseth:

That Whereas, The said United Mercury Mines Company, a corporation, is the owner (except as against the paramount title of the United States) of three groups of lode and placer mining claims situated in the Yellow Pine Mining District, Valley County, State of Idaho, commonly called the Cinna-

Defendant's Exhibit No. 4—(Continued)
bar Group, the Meadow Creek Group and the Antimony Group, comprising lode and placer mining claims, and comprising the following named mining claims, the notices of location of which are of record in the office of the County Recorder of Valley County, State of Idaho, at the book and page as herein stated, to wit:

Description of Claims

Cinnabar Group

Flyer: Amended, Book 6, Quartz, Page 75.

Emerald No. 1: Original, Book 3, Quartz, Page 396.

Emerald No. 2: Original, Book 3, Quartz, Page 398.

North Star Fraction: Original, Book 3, Quartz, Page 614.

Hard Climb No. 1: Amended, Book 6, Quartz, Page 87.

Hard Climb No. 2: Amended, Book 6, Quartz, Page 88.

Hard Climb No. 3: Amended, Book 6, Quartz, Page 89.

Hard Climb No. 4: Amended, Book 6, Quartz, Page 90.

Mountain Ridge No. 1: Amended, Book 6, Quartz, Page 77.

Mountain Ridge No. 2: Amended, Book 6, Quartz, Page 78.

Mountain Ridge No. 3: Amended, Book 6, Quartz, Page 79.

Defendant's Exhibit No. 4—(Continued)

Mountain Ridge No. 4: Amended, Book 6, Quartz,
Page 80.

Midnight No. 1: Amended, Book 6, Quartz,
Page 98.

Midnight No. 2: Amended, Book 6, Quartz,
Page 99.

Smith Extension No. 1: Amended, Book 6,
Quartz, Page 81.

Smith Extension No. 2: Amended, Book 6,
Quartz, Page 82.

Smith Extension No. 3: Amended, Book 6,
Quartz, Page 83.

Smith Extension No. 4: Amended, Book 6,
Quartz, Page 84.

Smith Extension No. 5: Amended, Book 6,
Quartz, Page 85.

Smith Extension No. 6: Amended, Book 6,
Quartz, Page 86.

Hermes: Patented, Book 4, Quartz, Page 194.

Pretty Maid: Patented, Book 4, Quartz, Page 195.

Annie Sell, Patented, Book 4, Quartz, Page 188.

Vermillion: Patented, Book 4, Quartz, Page 192.

Golden Gate No. 4: Patented, Book 4, Quartz,
Page 191.

Vermillion Extension No. 1: Patented, Book 4,
Quartz, Page 190.

Gold King: Amended, Book 6, Quartz, Page .

Gold King No. 1: Amended, Book 6, Quartz,
Page 96.

Gold King No. 2: Amended, Book 6, Quartz,
Page 97.

Defendant's Exhibit No. 4—(Continued)

Gold King No. 3: Amended, Book 6, Quartz, Page 100.

Monumental No. 1: Amended, Book 6, Quartz, Page 71.

Monumental No. 2: Amended, Book 6, Quartz, Page 70.

Monumental No. 3: Original, Book 3, Quartz, Page 516.

Monumental No. 4: Original, Book 3, Quartz, Page 512.

Monumental No. 5: Original, Book 3, Quartz, Page 511.

Monumental No. 6: Original, Book 3, Quartz, Page 509.

Monumental No. 7: Original, Book 3, Quartz, Page 600.

West Side No. 1: Amended, Book 6, Quartz, Page 94.

West Side No. 2: Amended, Book 6, Quartz, Page 95.

Golden Gate No. 1: Amended, Book 6, Quartz, Page 73.

Golden Gate No. 2: Original, Book 3, Quartz, Page 475.

Golden Gate No. 3: Original, Book 3, Quartz, Page 474.

El Rey: Amended, Book 6, Quartz, Page 104.

Quicksilver Queen No. 1: Original, Book 3, Quartz, Page 578.

Quicksilver Queen No. 2: Original, Book 3, Quartz, Page 577.

Defendant's Exhibit No. 4—(Continued)

First National No. 1: Amended, Book 6, Quartz,
Page 74.

Liberty: Amended, Book 6, Quartz, Page 101.

Liberty No. 1: Amended, Book 6, Quartz, Page
102.

U. S. A.: Amended, Book 6, Quartz, Page 76.

High Rock No. 1: Amended, Book 6, Quartz,
Page 53.

High Rock No. 2: Amended, Book 6, Quartz,
Page 54.

High Rock No. 3: Amended, Book 6, Quartz,
Page 55.

High Rock No. 4: Amended, Book 6, Quartz,
Page 56.

High Rock No. 5: Amended, Book 6, Quartz,
Page 57.

Victor No. 1: Original, Book 3, Quartz, Page 453.

Victor No. 2: Original, Book 3, Quartz, Page 455.

Victor No. 3: Original, Book 3, Quartz, Page 456.

Victor No. 4: Original, Book 3, Quartz, Page 458.

Victor No. 5: Original, Book 3, Quartz, Page 459.

Monumental Quicksilver: Amended, Book 6,
Quartz, Page 72.

Mountain Chief No. 1: Amended, Book 6, Quartz,
Page 58.

Mountain Chief No. 2: Amended, Book 6, Quartz,
Page 59.

Mountain Chief No. 3: Amended, Book 6, Quartz,
Page 60.

Mountain Chief No. 4: Amended, Book 6, Quartz,
Page 61.

Defendant's Exhibit No. 4—(Continued)

Mountain Chief No. 5: Amended, Book 6, Quartz, Page 62.

Mountain Chief No. 6: Amended, Book 6, Quartz, Page 63.

Mountain Chief No. 7: Amended, Book 6, Quartz, Page 64.

White Metal: Amended, Book 6, Quartz, Page 46.

White Metal No. 1: Amended, Book 6, Quartz, Page 47.

White Metal No. 2: Amended, Book 6, Quartz, Page 48.

White Metal No. 3: Amended, Book 6, Quartz, Page 49.

White Metal No. 4: Amended, Book 6, Quartz, Page 50.

White Metal No. 5: Amended, Book 6, Quartz, Page 51.

White Metal No. 6: Amended, Book 6, Quartz, Page 52.

Mountain Bell: Original, Book 3, Quartz, Page 325.

Mountain Bell Fraction: Original, Book 3, Quartz, Page 468.

Mountain Bell No. 1: Original, Book 3, Quartz, Page 470.

Vermillion Extension No. 2: Amended, Book 6, Quartz, Page 91.

Vermillion Extension No. 3: Amended, Book 6, Quartz, Page 92.

Vermillion Extension No. 4: Amended, Book 6, Quartz, Page 93.

Defendant's Exhibit No. 4—(Continued)

West End: Amended, Book 6, Quartz, Page 103.
Friends No. 1: Original, Book 5, Quartz, Page 75.
Friends No. 2: Original, Book 5, Quartz, Page 69.
Friends No. 3: Original, Book 5, Quartz, Page 74.
Friends No. 4: Original, Book 5, Quartz, Page 68.
North Star No. 1: Amended, Book 6, Quartz,
Page 65.

North Star No. 2: Amended, Book 6, Quartz,
Page 66.

North Star No. 3: Amended, Book 6, Quartz,
Page 67.

North Star No. 4: Amended, Book 6, Quartz,
Page 68.

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- Pat No. 17: Original, Book 4, Quartz, Page 555.
- Pat No. 18: , Book , Quartz, Page .
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- M. W. No. 3: Original, Book 4, Quartz, Page 505.
- M. W. No. 4: Original, Book 4, Quartz, Page 507.
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Y. P. C. No. 16: Original, Book 2, Placer, Page 543.

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Nora No. 6: Original, Book 7, Quartz, Page 140.
Nora No. 7: Original, Book 7, Quartz, Page 141.
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Bell No. 11: Original, Book , Quartz, Page .
Bell No. 12: Original, Book , Quartz, Page .
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North Bell No. 4: Original, Book , Quartz, Page .
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North Bell No. 10: Original, Book , Quartz,
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North Bell No. 11: Original, Book , Quartz,
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North Bell No. 12: Original, Book , Quartz,
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M. B. No. 7: Original, Book , Quartz, Page .

M. B. No. 8: Original, Book , Quartz, Page .

M. B. No. 9: Original, Book , Quartz, Page .

M. B. No. 10: Original, Book , Quartz, Page .

All of which records are hereby referred to for a more particular description of said mining claims;

And Whereas, The United Mercury Mines Company, a corporation, did on or about the 5th day of August, 1927, enter into an option agreement with F. W. Bradley of San Francisco, which said option agreement pertained to the said Cinnabar and Meadow Creek Groups of lode and placer claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, said option contract having been assigned by said F. W. Bradley to the Yellow Pine Company, a corporation, copies of which option agreement and said assignment are attached hereto and marked Exhibits A and B, respectively;

And Whereas, The party of the second part went

Defendant's Exhibit No. 4—(Continued)
into actual possession of said properties and began bona fide development work thereon upon the signing of and in accordance with the provisions of said option agreement dated August 5th, 1927, and has during each and every year thereafter expended in developing and equipping in, upon, and/or for the benefit of said properties a sum of not less than Twenty Four Thousand (\$24,000.00) Dollars;

And Whereas, The party of the second part has in accordance with the provisions of said option agreement dated August 5th, 1927, performed the necessary annual assessment work during each and every year from the date of said option agreement;

And Whereas, The party of the second part did upon signing and in accordance with the said option agreement dated August 5th, 1927, pay unto the said first party or for its use and benefit the sum of Two Thousand One Hundred Forty Seven and 75/100 (\$2,147.75) Dollars;

And Whereas, The party of the second part did pay to the said first party or for its use and benefit, the sum of Ten Thousand (\$10,000.00) Dollars on or before the first day of August, 1928, and also the sum of Ten Thousand (\$10,000.00) Dollars on or before the first day of February, 1929, in accordance with the provisions of said option agreement dated August 5th, 1927;

And Whereas, The party of the second part has in each and every other respect complied with all the terms and conditions of said option agreement dated August 5th, 1927, from the date thereof;

Defendant's Exhibit No. 4—(Continued)

And Whereas, The said United Mercury Mines Company, a corporation, and the said Yellow Pine Company, a corporation, did by a supplemental agreement entitled "Addenda To Agreement And Option Dated August 5th, 1927, Between The United Mercury Mines Company and F. W. Bradley Relating To The Cinnabar And Meadow Creek Groups Of Lode Mining Claims", and dated the first day of February, 1928, further modify and change certain parts of said option contract dated the 5th day of August, 1927, copy of which supplemental agreement is attached hereto and marked Exhibit C.

And Whereas, The said option contract dated August 5th, 1927, was further modified and changed in certain parts by a supplemental agreement dated the 30th day of August, 1929, by and between the said United Mercury Mines Company, a corporation, and the said Yellow Pine Company, a corporation, copy of which supplemental agreement is attached hereto and marked Exhibit D;

And Whereas, The said United Mercury Mines Company, a corporation, and the said Yellow Pine Company, a corporation, desire, each for itself, further changes, additions, and modifications in and to said option agreement dated August 5th, 1927, and said supplemental agreements dated February 1st, 1928, and August 30th, 1929, Exhibits C and D respectively, attached hereto;

And Whereas, The said United Mercury Mines Company, a corporation, and the said Yellow Pine

Defendant's Exhibit No. 4—(Continued)

Company, a corporation, further desire to express (a) the covenants and agreements made and entered into by the said option agreement dated August 5th, 1927, and (b) the modifications of which as expressed in the said supplemental agreements dated February 1st, 1928, and August 30th, 1929, respectively, and (c) further changes, additions and modifications in a single instrument of option contract and agreement for the purpose of clarity and convenience of reference;

Now, Therefore, For and in consideration of the premises and the mutual covenants herein contained, and for the sum of Ten (\$10.00) Dollars, paid by the party of the second part, the receipt whereof by the party of the first part is hereby acknowledged, it is mutually covenanted, agreed and understood by and between the parties hereto as follows:

I.

It is hereby specifically understood and agreed that this instrument of option contract and agreement rescinds, nullifies, supersedes and takes the place of all other contracts and agreements, whether attached hereto as exhibits or not, between the parties hereto, and that all negotiations between the parties hereto relative to the hereinbefore described properties, whether written or oral of any kind or character, are merged herein, and that this agreement is to be construed without reference to any of said former agreements or negotiations.

Defendant's Exhibit No. 4—(Continued)

Merger of Negotiations

II.

The said party of the first part does hereby grant and accord unto the said party of the second part, the sole and exclusive right, privilege and option to purchase all of the right, title and interest of the first party in and to the following:

Option Given

(a) Said Cinnabar and Meadow Creek and Antimony Groups of mining claims as hereinbefore described.

(b) Together with all dips, spurs and angles of all lodes therein.

(c) Together with all other mining claims now owned by or that may hereafter be located or acquired by said first party during the life of this agreement within 1500 linear feet of the extreme exterior boundaries of the said Cinnabar, Meadow Creek and Antimony Groups of mining claims, or within, or adjacent, or contiguous thereto.

(d) Together with the tenements, hereditaments and appurtenances and rights and privileges thereunto belonging or in any wise appertaining.

(e) Together with the personal property belonging to said first party situate upon or in said claims.

(f) And together with all mill sites, water rights, tail races, tailing sites, and tailing dams or easements that are now owned or may in the future be acquired by said first party for use in connection with said claims, or any of them.

Defendant's Exhibit No. 4—(Continued)
Purchase Price

The purchase price for all of which to be the sum of One Million Five Hundred Fifty Thousand (\$1,550,000.00) Dollars, lawful money of the United States of America, said sum to be paid (subject to the right of the second party to discontinue this agreement and to be relieved from further obligation to proceed hereunder as set forth in Paragraph XVI hereof) at the times and in the manner hereinafter provided, and said option to be subject at all times to the terms, covenants and provisions hereinafter expressed.

III.

The said party of the first part does hereby give, grant and accord unto the said party of the second part, or its representative or representatives, the sole and exclusive option, privilege and right to enter in and upon and to continue with the actual possession of said mining claims and work in and on them for the purpose of developing, equipping and extracting ores or metals from said claims, and in the manner and to the extent and at such places as may in the judgment of said second party be best suited to the best interests of both parties hereto, said option, however, to be subject at all times to the terms, covenants and provisions hereinafter expressed.

IV.

Development Work

The party of the second part hereby agrees, in

Defendant's Exhibit No. 4—(Continued)

the event it continues to exercise its rights under this option, to do and perform (subject always to the right of the second party to discontinue this agreement and to be relieved from any further obligation to proceed hereunder as set forth in Paragraph XVI hereof) the following:

(a) To perform and complete upon, or in or for the benefit of said claims, prior to the first day of May of each and every year that said second party remains in or is entitled to possession of said properties under the terms of this agreement, the necessary annual assessment work to hold and protect said claims under the mining laws of the United States and the State of Idaho, and to file and record, on or before the first day of June of each and every year during the occupation of said premises by said second party under the provisions of this agreement, in the office of the county Recorder of Valley County, State of Idaho, on behalf of the first party, the necessary proofs of such annual labor or assessment work upon said mining claims.

(b) To spend in, upon, or for the benefit or account of said properties, annually during the life of this agreement, the sum of at least Twenty Four Thousand (\$24,000.00) Dollars, said sum to include but not necessarily in addition to, such sums required for annual assessment work as provided in Paragraph (a) immediately preceding.

(c) To pay to the party of the first part at the times and in the manner hereinafter provided a royalty to apply on purchase price, based on a

Defendant's Exhibit No. 4—(Continued)

percentage of the Net Proceeds as determined by the difference between Gross Proceeds and Operating Costs, said net proceeds, gross proceeds and operating costs being more explicitly defined hereinafter, and said percentage of net proceeds to be determined in the following manner:

Certain Terms Defined

First: At the end of every calendar month, during the life of this agreement, the aggregate Total Capital Investment of the second party shall be computed, and also the aggregate total Net Proceeds, from the beginning to even date shall be computed, and, at any time when at the end of each successive calendar month, the sum of such aggregate Total Capital Investment so computed plus est at the rate of eight (8%) per cent on the Net Capital Investment as hereinafter defined, shall exceed the share of second party in the aggregate amount of total Net Proceeds, likewise computed of even date, then, in such event and whether such excess shall have been continuous from month to month or intermittent during such months, said second party shall pay to said first party, at the times and in the manner hereinafter provided, a royalty for the month last past as of the date of such computation, twenty (20%) per cent of the said monthly net proceeds, if any, for the said month last past, and the second party shall be entitled to keep for its own use and benefit the remaining eighty (80%) per cent of said monthly net

Defendant's Exhibit No. 4—(Continued)

proceeds; the terms Total Capital Investment, Net Capital Investment and Net Proceeds being more explicitly defined hereinafter; provided that when the share of second party in such aggregate amount of Net Proceeds so computed as aforesaid shall exceed the Total Capital Investment plus interest at eight (8%) per cent on the said Net Capital Investment as and when computed as aforesaid, then the said royalty for such month shall be fifty (50%) per cent of said monthly net proceeds, if any, computed and payable as aforesaid, said second party retaining for its own use and benefit the remaining fifty (50%) per cent of such monthly net proceeds.

Manner of Payment

Said royalty to be deposited by the second party in the Crocker First National Bank of San Francisco, California, to and for the credit and order of the said first party on or before the twentieth (20th) day of the calendar month next succeeding the receipt of said net proceeds by the second party, and the same to be so paid each and every month when there are any net proceeds until the purchase price of the said mining claims and properties has been completed as herein provided.

Gross Proceeds

By the term Gross Proceeds as used in this agreement is meant and intended such sums of money as may be received by the said second party from the sale of ores, concentrates and/or metals or other

Defendant's Exhibit No. 4—(Continued)
products derived by the second party from said properties under the terms of this agreement.

Operating Costs

By the term Operating Costs as used in this agreement is meant and intended all moneys expended by the said second party in the operation, maintenance and repairs of mine, mill, power and/or other plants and equipment operated in, upon or for the benefit and account of said properties or the mining operations hereof, and in preparatory mining, stoping and extraction of ores from said claims, and for the transportation, marketing, smelting and/or refining of ores, concentrates, metals and/or other products derived from said claims, and for taxes, insurance, supervision, legal and other reasonable overhead costs incurred by second party by reason of its possession and/or operation of said properties, plants and equipment. Said operating costs to be the actual cash cost to second party for labor, materials, insurance, taxes, transportation and/or other items of expense necessary to or required for or by reason of the possession of said premises and the production and marketing of said products derived from said claims by second party under the terms of this agreement.

Net Proceeds

By the term Net Proceeds, as used in this agreement, is meant and intended the difference between such sums received by second party under the term

Defendant's Exhibit No. 4—(Continued)

and above definition of gross proceeds and such sums of money expended by the second party under the term and above definition of operating costs.

Total Capital Investment

By the term Total Capital Investment, as used in this agreement, is meant and intended any and all moneys expended by the second party in, upon and/or for the benefit and/or account of said properties for the following purposes:—

(a) For mine, mill, power, and/or other plants and equipment including tunnels, roads, pipe lines, power lines, flumes and ditches, and all additions and improvements adding to the value or capacities thereof.

(b) For the search for and development of ore bodies within said mining claims.

(c) For the examination of said properties, research or experimental work upon ores from said claims, legal work in connection with titles and agreements appertaining to said properties, assessment work, insurance, taxes, supervision and/or any and all other general expenses incurred by the second party for the benefit or account of said properties.

Net Capital Investment

By the term Net Capital Investment, as used in this agreement, is meant and intended that sum of money which at the end of any calendar month during the life of this agreement shall be the difference or balance between the sum of such moneys expended by the second party under the foregoing

Defendant's Exhibit No. 4—(Continued)

term and definition of total capital investment and (in accordance with the first provision of Paragraph IV-c, page 15 of this agreement) the sum of such moneys as may have been received by the second party under the foregoing term and definition of net proceeds. Interest of said net capital investment as above defined shall be computed on the same during the life of this agreement as of and on the last day of each and every calendar month in which there remains or occurs a sum of money termed and defined as net capital investment, said interest to be computed against said net capital investment at the rate of eight (8%) per cent per annum and at the end of each calendar year said interest as computed against said monthly balances shall be added to said net capital investment and become a part thereof.

Improvements Not Severable

(d) That the second party will not remove any machinery, building or other equipment now situate upon or used in connection with the hereinbefore described properties and that it will keep the same in good condition and repair at its own expense, and the second party also agrees that all improvements made and buildings placed upon said premises by the second party shall become appurtenant thereto, and in the event the second party does not complete the purchase of said properties under the terms of this agreement and in case of termination, cancellation or forfeiture hereof or

Defendant's Exhibit No. 4—(Continued)

under, the said improvements and buildings shall become the property of the first party, provided, second party may remove severable machinery and supplies installed or placed upon said property by second party.

No Liens Allowable

(e) That the second party will keep said properties and the whole thereof free and clear of all liens of whatsoever kind or character, and the second party hereby covenants for itself and its successors and assigns, to hold the first party harmless from any and all liens and claims of whatsoever kind or nature, for wages or supplies, or any indebtedness whatsoever created by said second party by reason of its possession of, or its working of said claims. That the second party shall not be deemed or considered the agent of the first party under the provisions of the Statutes of Idaho relating to liens or otherwise, except for the performance by second party of said annual assessment work.

Notices to Be Posted

(f) That the second party hereto will make the necessary affidavits and post and record the necessary notices to comply with the provisions of Section 2311, Idaho Compiled Statutes and the laws of the State of Idaho, so as to notify all persons that the operations to be carried on under this agreement shall be at the sole cost and expense of the second party, and that the first party hereto shall not be responsible or liable in any way for

Defendant's Exhibit No. 4—(Continued)

the debts and obligations of the second party, and that contracts for labor, supplies or material by the second party shall not bind the first party or the hereinbefore described mining properties, or any part thereof, and that full compliance with the Statutes of the State of Idaho in regard to the making and filing and recording of the notices to effectuate this purpose shall be had immediately upon the second party entering into the possession of said property.

Work in Miner-like Manner

(g) To perform all work done upon said mining claims during the existence of this agreement in a proper and miner-like manner and that all workable tunnels and raises now existing thereon and all tunnels constructed thereunder shall be kept open, passable, properly timbered, and in shape by second party and that all stakes and monuments marking said claims shall be kept up and marked.

Taxes

(h) To pay, prior to delinquency all taxes of every kind and character that may be levied or assessed against said property during the life of this agreement.

V.

Deed in Escrow

The said party of the first part does hereby covenant and agree with the said party of the second part to do and perform the following things con-

Defendant's Exhibit No. 4—(Continued)

currently with the execution of this agreement, to-wit:

(a) To execute a good and sufficient deed or deeds granting and conveying to said second party all the right, title and interest of the said first party in and to said Cinnabar, Meadow Creek and Antimony Groups of mining claims and the whole thereof (except as against the paramount title of the United States of America) together with the buildings and improvements and personal property of said first party situate in or upon or appertaining to said claims, and to deposit in escrow with the Crocker First National Bank of San Francisco, California, said deed or deeds with appropriate instructions to said Bank to deliver said deed or deeds to the said second party upon the performance by it of all the terms and conditions of this agreement and the payment in full of One Million Five Hundred Fifty Thousand (\$1,550,000.00) Dollars, as herein provided.

(b) To execute and acknowledge such statement or statements as may be desired by the said second party to be recorded in the office of the County Recorder of Valley County, Idaho, showing the giving of the hereinbefore described options.

VI.

The said party of the first part does hereby further covenant and agree, to-wit:

(a) Upon the demand of the said second party to make and execute and place in escrow with the

Defendant's Exhibit No. 4—(Continued)
said Crocker First National Bank of San Francisco, California, any further deeds, instruments, conveyances or writings of whatsoever character that may be required by the said second party in order to convey to it all the right, title and interest in and to said group of claims and any and all claims that may hereafter be located within the exterior boundaries of said Cinnabar, Meadow Creek and Antimony Groups of mining claims or within 1500 feet of the exterior limits thereof.

VII.

It is further stipulated and agreed by and between the parties hereto that the purchase price for the said mining claims shall be the sum of One Million Five Hundred Fifty Thousand \$1,550,000.00) Dollars.

VIII.

Payment Condition Precedent to Delivery

It is further stipulated and agreed by and between the parties hereto that the payment of said purchase price is a condition precedent to the delivery of any deed or deeds for said property, and that the deed or deeds for said mining claims and properties shall be delivered to second party upon the payment to first party of the said sum of One Million Five Hundred Fifty Thousand (\$1,550,000.00) Dollars.

IX.

Advance of \$11,000.00

It is further stipulated and agreed by and be-

Defendant's Exhibit No. 4—(Continued)

tween the parties hereto that upon the execution of this agreement, second party will advance to first party the sum of Eleven Thousand (\$11,000.00) Dollars, the same to draw interest at the rate of eight (8%) per cent per annum and to be considered as a capital investment by second party as that term is hereinbefore defined and to be repaid second party in the same manner as any other capital invested by second party under this agreement.

X.

It is further stipulated and agreed by and between the parties hereto that all royalties and/or any and all other payments made to the first party by the second party in accordance with this and/or the said preceding agreements and/or addendas thereto, shall be applied to and constitute a part payment of the said purchase price, and the said first party hereby acknowledges the receipt of the sum of Thirty Three Thousand One Hundred Forty Seven and 75/100 (\$33,147.75) Dollars as having been received by it from the second party hereto as part payment on said purchase price.

XI.

Abstracts

It is further stipulated and agreed that within ninety days after written demand therefor, by the party of the second part to the party of the first part, the said party of the first part shall deliver to the Crocker First National Bank of San Fran-

Defendant's Exhibit No. 4—(Continued)

cisco, California, for delivery to the party of the second part, or its assigns, abstracts of title for the above described property. It is agreed that the party of the second part, or its assigns, shall have a period of ninety (90) days after said abstracts are delivered to said Crocker First National Bank for the examination of said abstracts of title, and at or before the end of said ninety days shall deliver to the party of the first part a written opinion containing all material objections that said party of the second part may raise to the title (except the paramount right of the United States) of the party of the first part to said claims, and the party of the first part shall have ninety days within which to correct such material defects in said possessory right, unless, in order to correct such defects, it is necessary to bring suit or suits to quiet title, in which event a reasonable time shall be allowed the party of the first part therefor, it being understood that the corrections of such defects are not precedent nor dependent conditions to the making of the payments and the performance of the conditions herein by the party of the second part to be kept and performed.

In the event second party shall fail to deliver written objections as and within the time aforesaid, or if first party shall make corrections as aforesaid, the second party or its assigns shall be conclusively held to have accepted and approved the title as such, as first party hereunder has agreed, upon performance of this option, to convey.

Defendant's Exhibit No. 4—(Continued)

XII.

It is further agreed and understood that there are certain claims of liens against said Hermes claim which are now in litigation, totaling not to exceed the sum of Sixty Thousand (\$60,000.00) Dollars, and which first party believes to be fraudulent and without foundation (the District Court of Valley County, Idaho, having already held one of said liens to be void and fraudulent) and said first party agrees to pay and discharge all of said liens, together with legal interest and costs of respective suits, when and if they are finally decided by the Supreme Court of Idaho to be valid. In order to protect its right to possession second party may pay any judgment against, or redeem such property from any sale under said liens and deduct the cost thereof from the next payment due from it thereafter.

XIII.

New Claims

It is agreed that first party at all times during the existence of this contract, shall have free access to the above described properties for the purpose of inspecting said properties and making surveys, setting stakes and amending and making locations; that all amended locations made, as well as all locations of new claims and of fractional claims, within or upon the lands embraced in or within fifteen hundred (1500) feet of the general exterior lines of the general groups of claims above or within described, and all locations of millsites, power

Defendant's Exhibit No. 4—(Continued)

plants, sites and water rights made either by first party or second party or its assigns, prior to delivery of conveyance hereunder, shall be made in the name of and for the party of the first part, and that all such new and amended locations shall be deemed and considered as included in this option and as part of the property to be conveyed to second party and no additional price shall be paid therefor, in case the payments hereinbefore described are made at the time and at the place and in the manner herein described. The party of the first part agrees that, upon the written demand of the party of the second part, it will make and execute and place in escrow in said Crocker First National Bank of San Francisco, California, a deed or deeds covering and conveying all of said new locations and filings to the party of the second part, to be held by said Bank subject to the terms and conditions of this option.

XIV.

Patents

The party of the first part agrees that upon the written demand of second party, it will, in its own name, apply for United States Patent or Patents for the above described mining claims, the same to be secured, however, at the expense of the second party.

XV.

Modification in Writing Waivers

It is further stipulated and agreed that no modification shall be of any force or effect or binding

Defendant's Exhibit No. 4—(Continued)

upon either or any of the parties hereto unless made in writing and signed by both parties hereto; and that the waiver by first party of any breach of any one or more covenants shall not be construed as a waiver of the breach of any covenant, nor of time as of the essence hereof.

XVI.

Forfeiture

It is hereby expressly stipulated and agreed that this is an option contract and not a contract of purchase, and not a buy and sell agreement, nor a contract of or to purchase, and that time is of the essence of this contract, and that in the event the party of the second part fails to perform the conditions of this agreement strictly according to the terms hereof, or fails to keep each and every covenant by it to be kept, and fails within 60 days after the receipt of notice and demand from first party to keep and perform any covenant herein by it to be kept and performed, then in that event, all the right of the party of the second part, and its assigns, shall at the option of the party of the first part terminate, and all the payments and improvements which shall have been made by the party of the second part, or its assigns, and all buildings erected or used as hereinbefore provided, shall in such event be forfeited to the party of the first part, and that said payments and improvements shall be considered as liquidated damages, the manner of ascertaining the actual damages being difficult, provided, however, that in the event

Defendant's Exhibit No. 4—(Continued)

second party desires at any time to be relieved from further obligation to proceed under this agreement it shall give notice in writing to that effect by United States mail, postage prepaid, or by telegram to the party of the first part, or shall serve upon first party at 605 Eastman Building, Boise, Idaho, and upon the Crocker First National Bank of San Francisco, California, a written notice of its intention not to proceed further under this agreement, and shall thereafter be relieved from all obligation to proceed under, and from any and all liability on account of any omission thereafter, any thing herein to the contrary notwithstanding; that said Crocker First National Bank of San Francisco shall return the deed to first party herein provided for, and the same shall be null and void.

XVII.

Surrender of Possession

It is further stipulated and agreed that upon the failure of the party of the second part to perform any terms or conditions of this contract, it will, upon the demand of the first party, at once surrender said premises to the party of the first part.

XVIII.

Inspection of Claims and Work

It is specifically agreed that during the existence of this contract, and during the time the party of the second part shall have the right to the possession of said property under this contract, the party of the first part, its agents and representatives,

Defendant's Exhibit No. 4—(Continued)

shall have at all reasonable times free access to said property and the whole thereof, for the purpose of inspecting the nature, character and quantity of work being performed by the party of the second part thereon, but such inspection shall be conducted in such manner as not to interfere with the work of the party of the second part.

XIX.

Inspection of Books

The party of the second part hereby agrees to furnish all information, including smelter returns, correspondence and bank statements which first party may require in order to assure it that it is receiving the amount of royalty or net proceeds of said property as herein provided for. Second party further agrees to render to first party at Boise, Idaho, on the 20th day of each month, a statement which shall fully set forth the full particulars of the operations of the preceding month, and at the same time making such purchase price payments as may then be due under the terms of this agreement, and the party of the first part, at reasonable times, or at least every six months, shall have access to the books of account of the party of the second part relating to the operation of said property for the purpose of inspection.

XX.

Assignment

It is further expressly agreed and covenanted

Defendant's Exhibit No. 4—(Continued)

that this agreement is assignable by second party, and that this agreement and all its terms and conditions shall be binding upon the heirs, successors and assigns of both the parties hereto; provided, however, that in the event the second party makes an assignment of this option, its assignee or assignees shall, by the taking of this agreement or assignment, assume all obligations to be performed hereunder by the second party, and thereupon the second party shall notify the first party in writing of such assignment, giving the name and address of such assignee or assignees, and from and after the receipt of such notice by the first party, second party shall be relieved from all liability on account of any act or omission on its part thereafter.

XXI.

It is further stipulated and agreed that in the event the party of the second part decides that any of the claims hereinbefore described do not have sufficient mineral to justify the development work or the doing of the annual assessment work thereon that such claims may be abandoned whenever first party consents thereto in writing, signed by the President and Secretary of the party of the first part.

UNITED MERCURY MINES
COMPANY, a Corporation,

/s/ By J. J. OBERBILLIG,
President.

Defendant's Exhibit No. 4—(Continued)

Attest:

/s/ J. F. KOELSCH, Secretary,
Party of the First Part.

YELLOW PINE COMPANY,
a Corporation,

/s/ By F. W. BRADLEY,
President.

Attest:

/s/ E. A. GRIFFEN, Secretary.
Party of the Second Part.

[Seal]

EXHIBIT A

Agreement

This agreement, made and entered into at San Francisco, California, this 5th day of August, 1927, by and between the United Mercury Mines Company, a corporation organized and existing under and by virtue of the laws of the State of Idaho with its principal office at Boise, Ada County, Idaho, the Party of the First Part, and F. W. Bradley, of San Francisco, the Party of the Second Part (said Party of the First Part acting herein pursuant to the authority of the Board of Directors), Witnesseth:

Description of Claims

That whereas, the party of the first part is the owner of (except as against the paramount title

Defendant's Exhibit No. 4—(Continued)
of the United States) and is entitled to and in possession of certain lode and placer mining claims situated in the Yellow Pine Mining District, Valley County, State of Idaho, commonly called the Cinnabar Group of Lode Mining Claims and the Meadow Creek Group of Lode and Placer Mining Claims, and comprising the following named mining claims, the notices of location of which are of record in the office of the County Recorder of Valley County, State of Idaho, in the Book and at the Page as herein stated, to-wit:

Cinnabar Group

Hermes: Book 4, Quartz, Page 194.

Pretty Maid: Book 4, Quartz, Page 195.

Vermillion: Book 4, Quartz, Page 188.

Flyer: Book 4, Quartz, Page 407.

Emerald No. 1: Book 3, Quartz, Page 396.

Emerald No. 2: Book 3, Quartz, Page 398.

North Star Fraction: Book 3, Quartz, Page 614.

Hard Climb No. 1: Book 5, Quartz, Page 31.

Hard Climb No. 2: Book 5, Quartz, Page 32.

Hard Climb No. 3: Book 5, Quartz, Page 33.

Hard Climb No. 4: Book 5, Quartz, Page 34.

Mountain Ridge No. 1: Book 5, Quartz, Page 30.

Mountain Ridge No. 2: Book 5, Quartz, Page 28.

Mountain Ridge No. 3: Book 5, Quartz, Page 29.

Mountain Ridge No. 4: Book 5, Quartz, Page 27.

Midnight No. 1: Book 3, Quartz, Page 445.

Midnight No. 2: Book 3, Quartz, Page 447.

Defendant's Exhibit No. 4—(Continued)

Smith Extension No. 1: Book 3, Quartz, Page 567.

Smith Extension No. 2: Book 3, Quartz, Page 568.

Smith Extension No. 3: Book 3, Quartz, Page 573.

Smith Extension No. 4: Book 3, Quartz, Page 569.

Smith Extension No. 5: Book 3, Quartz, Page 571.

Smith Extension No. 6: Book 3, Quartz, Page 572.

Annie Sell: Amended, Book 4, Quartz, Page 192.

Gold King: Book 3, Quartz, Page 337.

Gold King No. 2: Book 3, Quartz, Page 327.

Gold King No. 1: Book 3, Quartz, Page 323.

Gold King No. 3: Book 4, Quartz, Page 6.

Monumental No. 1: Book 3, Quartz, Page 517.

Monumental No. 2: Book 3, Quartz, Page 513.

Monumental No. 3: Book 3, Quartz, Page 516.

Monumental No. 4: Book 3, Quartz, Page 512.

Monumental No. 5: Book 3, Quartz, Page 511.

Monumental No. 6: Book 3, Quartz, Page 509.

Monumental No. 7: Book 3, Quartz, Page 600.

West Side No. 1: Book 3, Quartz, Page 508.

West Side No. 2: Book 3, Quartz, Page 507.

Golden Gate No. 1: Book 3, Quartz, Page 476.

Golden Gate No. 2: Book 3, Quartz, Page 475.

Golden Gate No. 3: Book 3, Quartz, Page 474.

Golden Gate No. 4: Book 4, Quartz, Page 191.

El Roy: Book 3, Quartz, Page 433.

Defendant's Exhibit No. 4—(Continued)

Quicksilver Queen No. 1: Book 3, Quartz, Page 578.

Quicksilver Queen No. 2: Book 3, Quartz, Page 577.

First National No. 1: Book 3, Quartz, Page 402.

Liberty: Book 3, Quartz, Page 405.

Liberty No. 1: Book 3, Quartz, Page 406.

U. S. A.: Book 3, Quartz, Page 403.

High Rock No. 1: Book 3, Quartz, Page 489.

High Rock No. 2: Book 3, Quartz, Page 490.

High Rock No. 3: Book 3, Quartz, Page 491.

High Rock No. 4: Book 3, Quartz, Page 493.

High Rock No. 5: Book 3, Quartz, Page 494.

Victor No. 1: Book 3, Quartz, Page 453.

Victor No. 2: Book 3, Quartz, Page 455.

Victor No. 3: Book 3, Quartz, Page 456.

Victor No. 4: Book 3, Quartz, Page 458.

Victor No. 5: Book 3, Quartz, Page 459.

Monumental Quicksilver: Book 5, Quartz, Page 12.

Mountain Chief No. 1: Book 3, Quartz, Page 388.

Mountain Chief No. 2: Book 3, Quartz, Page 390.

Mountain Chief No. 3: Book 3, Quartz, Page 391.

Mountain Chief No. 4: Book 3, Quartz, Page 392.

Mountain Chief No. 5: Book 3, Quartz, Page 436.

Mountain Chief No. 6: Book 3, Quartz, Page 437.

Mountain Chief No. 7: Book 3, Quartz, Page 439.

White Metal: Book 3, Quartz, Page 324.

White Metal No. 1: Book 3, Quartz, Page 385.

White Metal No. 2: Book 3, Quartz, Page 386.

White Metal No. 3: Book 3, Quartz, Page 387.

White Metal No. 5: Book 3, Quartz, Page 395.

Defendant's Exhibit No. 4—(Continued)

White Metal No. 6: Book 3, Quartz, Page 394.

Mountain Bell: Book 3, Quartz, Page 325.

Mountain Bell Fraction: Book 3, Quartz, Page 468.

Mountain Bell No. 1: Book 3, Quartz, Page 470.

Vermilion Extension No. 1: Book 4, Quartz, Page 190.

Amended

Vermilion Extension No. 2: Book 5, Quartz, Page 70.

Vermilion Extension No. 3: Book 5, Quartz, Page 71.

Vermilion Extension No. 4: Book 5, Quartz, Page 72.

Friends No. 1: Book 5, Quartz, Page 75.

Friends No. 2: Book 5, Quartz, Page 69.

Friends No. 3: Book 5, Quartz, Page 74.

Friends No. 4: Book 5, Quartz, Page 68.

North Star No. 1: Book 3, Quartz, Page 460.

North Star No. 2: Book 3, Quartz, Page 461.

North Star No. 3: Book 3, Quartz, Page 463.

North Star No. 4: Book 3, Quartz, Page 464.

North Star No. 5: Book 3, Quartz, Page 465.

White Metal No. 4: Book 3, Quartz, Page 383.

And the West End lode mining claims the notice of location of which is of record in the office of the County Recorder of Idaho County, Idaho in Book 20 of Quartz Locations, at page 146.

Meadow Creek Group

Meadow Creek No. 1: Patented, Book 4, Page 118.

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Defendant's Exhibit No. 4—(Continued)

Meadow Creek No. 2: Patented, Book 4, Page 184.

Meadow Creek No. 3: Patented, Book 4, Page 185.

Meadow Creek No. 4: Patented, Book 4, Page 186.

Meadow Creek No. 5: Patented, Book 4, Page 187.

The United States Patent for the above described claims being of record in the office of the County Recorder of Valley County, Idaho in Book...of..., at page....

Meadow Creek No. 6: Book 5, Page 186.

Meadow Creek No. 7: Book 5, Page 187.

Meadow Creek No. 8: Book 5, Page 188.

Meadow Creek No. 9: Book 5, Page 189.

Meadow Creek No. 10: Book 5, Page 190.

Meadow Creek No. 11: Book 5, Page 191.

Meadow Creek No. 12: Book 5, Page 192.

Meadow Book No. 13: Book 5, Page 193.

Meadow Creek No. 14: Book 5, Page 194.

Meadow Creek No. 15: Book 5, Page 195.

Meadow Creek No. 16: Book 5, Page 196.

Meadow Creek No. 17: Book 5, Page 197.

Monday No. 1: Book 5, Page 423.

Monday No. 2: Book 5, Page 424.

Monday No. 3: Book 5, Page 425.

Monday No. 4: Book 5, Page 426.

Monday No. 5: Book 5, Page 427.

Monday No. 6: Book 5, Page 428.

Monday No. 7: Book 5, Page 429.

Defendant's Exhibit No. 4—(Continued)

Monday No. 8: Book 5, Page 430.

J. S.: Book 5, Page 160.

J. S. No. 2: Book 5, Page 161.

J. S. No. 3: Book 5, Page 162.

Bud No. 1: Book 5, Page 404.

Bud No. 2: Book 5, Page 405.

Bud No. 3: Book 5, Page 406.

Bud No. 4: Book 5, Page 407.

Bud No. 5: Book 5, Page 408.

Bud No. 6: Book 5, Page 409.

Bud No. 7: Book 5, Page 410.

Bud No. 8: Book 5, Page 411.

Bud No. 9: Book 5, Page 412.

Bud No. 10: Book 5, Page 413.

Bud No. 11: Book 5, Page 414.

Bud No. 12: Book 5, Page 415.

Bud No. 13: Book 5, Page 416.

Bud No. 14: Book 5, Page 417.

Bud No. 15: Book 5, Page 418.

Bud No. 16: Book 5, Page 419.

Bud No. 17: Book 5, Page 420.

Bud No. 18: Book 5, Page 421.

Bud No. 19: Book 5, Page 422.

Above all Quartz Locations.

Placer Locations

Meadow Queen No. 1: Book 2, Page 334.

Meadow Queen No. 2: Book 2, Page 304.

Meadow Queen No. 3: Book 2, Page 303.

East Fork No. 1: Book 2, Page 333.

East Fork No. 2: Book 2, Page 332.

Defendant's Exhibit No. 4—(Continued)

East Fork No. 3: Book 2, Page 331.

East Fork No. 4: Book 2, Page 330.

East Fork No. 5: Book 2, Page 329.

Meadow Creek No. 1: Book 2, Page 328.

Meadow Creek No. 2: Book 2, Page 327.

Meadow Creek No. 3: Book 2, Page 326.

Meadow Creek No. 4: Book 2, Page 314.

Meadow Creek No. 5: Book 2, Page 313.

Meadow Creek No. 6: Book 2, Page 312.

Meadow Creek No. 7: Book 2, Page 310.

Meadow Creek No. 8: Book 2, Page 309.

Meadow Creek No. 9: Book 2, Page 308.

Meadow Creek No. 10: Book 2, Page 306.

Meadow Creek No. 11: Book 2, Page 305.

Meadow Creek No. 12: Book 2, Page 315.

Meadow Creek No. 13: Book 2, Page 316.

Meadow Creek No. 14: Book 2, Page 317.

Meadow Creek No. 15: Book 2, Page 319.

Meadow Creek No. 16: Book 2, Page 318.

Meadow Creek No. 17: Book 2, Page 325.

Meadow Creek No. 18: Book 2, Page 324.

Meadow Creek No. 19: Book 2, Page 323.

Meadow Creek No. 20: Book 2, Page 322.

Meadow Creek No. 21: Book 2, Page 321.

Placer Queen: Book 2, Page 320.

All of which records are hereby referred to for a more particular description of said mining claims, and,

Whereas, the party of the second part desires to take possession of, occupy, mine and operate the said mining claims and to secure an exclusive op-

Defendant's Exhibit No. 4—(Continued)

tion to the right to purchase said mining claims, and the party of the first part is willing to grant, accord and agree to the same,

Now, therefore, for and in consideration of the premises and the sum of Ten and No/100 (\$10.00) Dollars, paid by the party of the second part, the receipt whereof by the party of the first part is hereby acknowledged, it is mutually covenanted, agreed and understood by and between the parties hereto as follows:

I.

The party of the first part does hereby grant and accord unto the second party the exclusive right, privilege, and option to purchase all the right, title and interest of the party of the first part in and to said mining claims above named, together with all dips, spurs, and angles of all lode claims thereof, together with all other mining claims now owned by or that may hereafter be located or acquired by the first party during the existence of this contract within 1500 feet of the exterior limits of the aforesaid Cinnabar Group and Meadow Creek Group or within or adjacent or contiguous thereto, together with the tenements, hereditaments, and appurtenances and right and privileges thereunto belonging or in any wise appertaining and the personal property situate upon or in said claims, and belonging to said first party, and together with all millsites, water rights, tail races, tailing sites, and tailing dams or easements that are now owned by or may be acquired by first party for use in con-

Defendant's Exhibit No. 4—(Continued)

nection with the above described claims or any of them for the sum of One Million Five Hundred Thousand (\$1,500,000.00) Dollars, lawful money of the United States of America, (subject to the right of the party of the second part to discontinue this agreement and to be relieved from further obligations to proceed hereunder as set forth hereunder in Paragraph XII, hereof) said sums to be paid at the times and in the manner hereinafter mentioned, and such option to be subject at all times to the terms, covenants, and provisions hereinafter expressed.

II.

Manner of Payment

The purchase price for all of the interests of the party of the first part in and to said properties is to be paid by the second party by his depositing to the credit of party of the first part in the Crocker First National Bank of San Francisco, California, until the purchase price of One Million Five Hundred Thousand (\$1,500,000.00) Dollars is paid; royalties from all ores, bullion, and minerals mined or taken from said claims as follows:

First: During the period from the date that production starts as hereinafter defined, and or until second party shall have been repaid his investment in said property with interest at 8% per annum a royalty of 20% of the net proceeds from any and all ore from said property shipped, mined, milled or treated shall be paid by second party to said

Defendant's Exhibit No. 4—(Continued)

Crocker First National Bank for the credit of the first party.

Second: Whenever second party shall have been repaid his investment in said properties together with interest thereon at 8% per annum, said second party shall pay to the first party a royalty of 50% of the net proceeds from any and all ore from said property shipped, mined, milled or treated after production starts, until the entire purchase price shall have been paid; said royalty to be paid by second party by his depositing the same in said Crocker First National Bank for credit of first party. It being understood and agreed by and between the parties hereto that production shall be deemed to have started whenever the party of the second part has erected and put in operation a reduction plant for handling quicksilver ore or reducing any of the ores from said properties; production shall also be deemed to have started whenever any commercial ore, bullion, metals or concentrates are taken from said properties.

Net Proceeds

By the term "net proceeds" as used in this instrument, is meant and intended the difference between the cash received from the sale of ore, bullion, metals or concentrates mined from or produced upon said properties, and the actual cash cost of producing the same; provided, however, that by the words "actual cash cost" is meant only the actual expenses for labor, supplies, materials, fuel,

Defendant's Exhibit No. 4—(Continued)

power and insurance and taxes required for mining, milling or for reducing and for transportation and marketing charges. Said royalties hereinbefore described to be paid party of first part, shall be deposited to the credit of the first party in said Bank on or before the 20th day of the month next succeeding the receipt of said proceeds by second party; the same to be paid each and every month after production starts, when there are any net proceeds as defined herein.

III.

It is further agreed, that the party of the second part, or his representative or representatives, upon the signing of this agreement, shall have the right, to enter into the actual possession of the above described mining claims, and work in and on them for the purpose of conducting mining operations and mining, and developing thereon in a prudent and miner-like manner, and that from the date hereof, and during all the time this agreement shall continue in force and effect, the party of the second part shall be entitled to the sole and exclusive possession of said properties and premises, and may work, mine and develop the same as he may deem advisable, subject to the terms hereinafter in Article V, contained.

IV.

It is further stipulated and agreed that all payments to be made under this agreement shall be made to the party of the first part in the banking

Defendant's Exhibit No. 4—(Continued)

house in the Crocker First National Bank at San Francisco, California, which bank is also agreed to be the escrow holder of this agreement and all papers to be placed in escrow hereunder.

V.

It is further stipulated and agreed that the party of the second part takes the possession of said property under this agreement, and acquires this option subject to the following terms and conditions, and the second party covenants and agrees:

(a) That he will go into the actual possession of said properties and commence bona fide development work thereon upon the signing of this agreement, and that during the year ending August 1st, 1928, and during each and every year thereafter he shall expend in developing, equipping and mining in and upon or for the benefit of said properties, the sum of Twenty-four Thousand (\$24,000.00) Dollars, subject to the provisions as to discontinuance and relief from the obligations to proceed further hereunder as set forth in Paragraph XII hereof, and that thereafter, during the life of this option he shall work and develop the same with an adequate force of men for economic mining, unless prevented by Acts of God, war, invasion, labor strikes, or other circumstances, acts or conditions beyond his control.

Development Work

(b) That prior to the first day of May, 1938,

Defendant's Exhibit No. 4—(Continued)

and of each and every year thereafter during the life of this agreement, he will perform development work on said mining claims, the same to be in such an amount and distributed over said groups so that each claim in said groups shall have at least \$100.00 worth of work performed for its benefit for the year ending July 1st, at 12:00 o'clock noon, 1928, and each and every year thereafter to the end that second party shall have fully performed all annual labor and assessment work now or hereafter required to be done by the laws of the State of Idaho and the United States; and the party of the second part shall, before the first of June, 1928, and before the first of June of each and every year thereafter, make, cause to be filed in the office of the County Recorder of Valley County, Idaho, on behalf of first party, the necessary proofs of annual labor or assessment work for said mining claims;

Improvements Not Severable

(c) That he will not remove any machinery, buildings or other equipment now situate upon or used in connection with the above described mining claims, that he will keep the same in good condition, and repair, at his own expense, and he agrees that all improvements, made and buildings placed on or used in connection with or for said property shall become appurtenant to the said property, and in the event the said party of the second part does not complete the purchase of said property under the terms of this agreement, and in

Defendant's Exhibit No. 4—(Continued)

case of termination, cancellation or forfeiture hereof or under; the said improvements of the buildings shall become the property of the party of the first part, provided, second party may remove severable machinery which he may install;

No Liens Allowable

(d) That he will keep said property and the whole thereof, free and clear of all liens of whatsoever kind or character, and the party of the second part hereby covenants for himself, and his heirs, legal representatives, successors and assigns, to hold the party of the first part harmless from any and all liens and claims of whatsoever kind or nature, for wages, or supplies, or any indebtedness whatsoever created by said party of the second part by reason of his possession of, or his working of said claims that second party shall not be deemed or considered the agent of the first party under the provisions of the Statutes of Idaho relating to liens or otherwise, except for the performance by him of said annual assessment work;

Notices to Be Posted

(e) That he will make the necessary affidavits and post and record the necessary notices to comply with the provisions of Section 2311 Idaho Compiled Statutes and the laws of the State of Idaho, so as to notify all persons that the operations to be carried on under this agreement shall at the sole cost and expense of the party of the second

Defendant's Exhibit No. 4—(Continued)

part, and that the party of the first part shall not be responsible or liable in any way for the debts and obligations of the party of the second part, and that contracts for labor, supplies or material by party of the second part shall not bind the party of the first part or the above described mining property, or any part thereof, and that full compliance with the Statutes of the State of Idaho in regard to the making and filing and recording of the notices to effectuate this purpose shall be had immediately upon the party of the second part entering into the possession of said property;

Work in Miner-like Manner

(f) That all the work done upon said mining claims during the existence of this agreement by said second party shall be done in a proper and miner-like manner and that all workable tunnels and raises now existing thereon, and all tunnels constructed thereunder, shall be kept open, passable, properly timbered, and in shape by second party, and that all stakes and monuments marking claims shall be kept up and marked.

(g) That upon the signing of this agreement the party of the second part will pay to the party of the first part or for its use and benefit the payroll of the party of the first part for the months of May, June and July, 1927, which said payroll amounts to the sum of \$2,147.75, as set forth in Exhibit "A" hereto attached.

Defendant's Exhibit No. 4—(Continued)

Taxes

(h) That he will pay, prior to delinquency all taxes of every kind and character that may be levied or assessed against said property for the year 1927, and thereafter during the life of this agreement.

(i) That on or before the first day of August, 1928, the said party of the second part shall pay to the said party of the first part or for its use and benefit, fifty (50%) per cent of the outstanding indebtedness of said party of the first part, the same being in the amounts and owing to the persons indicated in Exhibit "B" which is attached hereto, and that on or before the first day of February, 1929, shall pay the remainder of said indebtedness, provided, however, that on the payment of the said indebtedness or any part thereof, the party of the first part shall execute and deliver to the party of the second part its promissory note for the amount of said indebtedness so paid, the same to be in the following form:

\$..... Idaho 19....

On or before ten years after date, for value received, the United Mercury Mines Company, a corporation promises to pay to the order of at, Dollars, in lawful money of the United States of America, with interest thereon in like lawful money from date until paid at the rate of eight per cent per annum, interest to be paid at maturity.

Defendant's Exhibit No. 4—(Continued)

And in case suit or action is instituted to collect this note or any part thereon, the maker promises to pay, besides the costs and disbursements allowed by law, such additional sum as the court may adjudge reasonable as attorney's fees in said suit or action.

United Mercury Mines Company, a Corporation.

.....

President.

Attest:

.....

Secretary.

VI.

Deed in Escrow

It is further understood and agreed that concurrently with the execution of this agreement the party of the first part will execute a good and sufficient deed or deeds granting and conveying all the right, title and interest of first party in and to said property and the whole thereof (except as against the paramount title of the United States) to the party of the second part, his heirs, and assigns, and that this said deed, together with a copy of this agreement shall be delivered to the Crocker First National Bank of San Francisco, California, in escrow; said deed to be delivered to the party of the second part upon the performance by him of all the terms and conditions of this agreement and the payment in full of the One Million Five Hundred Thousand (\$1,500,000.00) Dollars, hereinbefore specified. Upon the failure of the party

Defendant's Exhibit No. 4—(Continued)

of the second part to perform any of the terms of this agreement by him to be performed, at the time and in the manner provided for in this agreement, the said Crocker First National Bank shall at once return said deed to the party of the first part.

VII.

Abstracts

It is further stipulated and agreed that within ninety days after written demand therefor, by the party of the second part to the party of the first part, the said party of the first part shall deliver to the Crocker First National Bank of San Francisco, California, for delivery to the party of the second part or his assigns, abstracts of title for the above described property. It is agreed that the party of the second part or his assigns, shall have a period of ninety (90) days after said abstracts are delivered to said Crocker First National Bank for the examination of said abstracts of title, and at, or before the end of said ninety days, shall deliver to the party of the first part a written opinion containing all material objections that said party of the second part may raise to the title (except the paramount right of the United States) of the party of the first part to said claims, and the party of the first part shall have ninety days within which to correct such material defects in said possessory right, unless, in order to correct such defects, it is necessary to bring suit or suits to quiet title, in which event a reasonable time shall

Defendant's Exhibit No. 4—(Continued)

be allowed the party of the first part therefor, it being understood that the corrections of such defects are not precedent nor dependent conditions to the making of the payments and the performance of the conditions herein by the party of the second part to be kept and performed.

In the event second party shall fail to deliver written objections as, and within the time aforesaid, or if first party shall make corrections as aforesaid, the second party or his assigns shall be conclusively held to have accepted and approved the title as such, as first party hereunder has agreed, upon performance of this option to convey.

VIII.

It is further agreed and understood, that there are certain claims of liens against said Hermes claim which are now in litigation, totaling not to exceed the sum of Sixty Thousand (\$60,000.00) Dollars, and which first party believes to be fraudulent and without foundation (the District Court of Valley County, Idaho, having already held one of said liens to be void and fraudulent) and said first party agrees to pay and discharge all of said liens, together with legal interest and costs of respective suits, when and if they are finally decided by the Supreme Court of Idaho to be valid; in order to protect its right to possession second party may pay any judgment against, or redeem such property from any sale under said liens and deduct the cost thereof from the next payment due from it thereafter.

Defendant's Exhibit No. 4—(Continued)

IX.

New Claims

It is agreed that first party at all times during the existence of this contract, shall have free access to the above described properties for the purpose of inspecting said properties and making surveys, setting stakes and amending and making locations; that all amended locations made, as well as all locations of new claims, and of fractional claims within or upon the lands embraced in or within, fifteen hundred (1500) feet of the general exterior lines of the general group of claims above or within described, and all locations of millsites, power plants, sites and water rights made either by first or second party or his assigns, prior to delivery of conveyance hereunder, shall be made in the name of, and for, the party of the first part, and that all such new and amended locations shall be deemed and considered as included in this option and as part of the property to be conveyed to second party and no additional price shall be paid therefor, in case the payments hereinbefore described are made at the time and at the place and manner herein described; the party of the first part agrees that, upon the written demand of the party of the second part it will make and execute and place in escrow in said Crocker First National Bank of San Francisco, a deed or deeds covering and conveying all of said new locations and filings to the party of the second part, to be held by said bank subject to the terms and conditions of this option.

Defendant's Exhibit No. 4—(Continued)

X.

Patents

Party of first part agrees that upon written demand of second party it will in its own name, apply for United States patent or patents for the above described mining claims, the same to be secured, however, at the expense of the second party.

XI.

Modification in Writing Waivers

It is further stipulated and agreed that no modification shall be of any force or effect or binding upon either or any of the parties hereto unless made in writing and signed by both parties hereto; and that the waiver by first party of any breach of any one or more covenants shall not be construed as a waiver of the breach of any covenant, nor of time as of the essence hereof.

XII.

Forfeiture

It is hereby expressly stipulated and agreed that this is an option contract and not a contract of purchase, and not a buy and sell agreement nor a contract of or to purchase, and that time is of the essence of this contract, and that in the event the party of the second part fails to perform the conditions of this agreement strictly according to the terms hereof, or fails to keep each and every covenant by him to be kept, then in that event, without demand or notice, all the right of the party

Defendant's Exhibit No. 4—(Continued)

of the second part, and his assigns, shall at the option of the party of the first part, terminate, and all the payments and improvements which shall have been made by the party of the second part, or his assigns, and all buildings erected or used as hereinbefore provided, shall in such event be forfeited to the party of the first part, and that said payments and improvements shall be considered as liquidated damages, the manner of ascertaining the actual damages being difficult; provided, however, that in the event second party desires at any time to be relieved from further obligation to proceed under this agreement he shall give notice in writing to that effect by United States mail, postage prepaid, or by telegram to the party of the first part or shall serve upon first party at 605 Eastman Building, Boise, Idaho, and upon the Crocker First National Bank of San Francisco, California, a written notice of his intention not to proceed further under this agreement, and shall thereafter be relieved from all obligation to proceed under and from any and all liability on account of any omission thereafter, anything herein to the contrary notwithstanding; that said Crocker First National Bank of San Francisco, shall return the deed to first party herein provided for, and the same shall be null and void.

XIII.

Surrender of Possession

It is further stipulated and agreed that upon the

Defendant's Exhibit No. 4—(Continued)

failure of the party of the second part to perform any terms or conditions of this contract he will at once surrender said premises to the party of first part.

XIV.

Inspection of Claims and Works

It is specifically agreed that during the existence of this contract, and during the time the party of the second part shall have the right to the possession of said property under this contract, the party of the first part, its agents and representatives shall have at all reasonable times, free access to said property and the whole thereof, for the purpose of inspecting the nature, character and quantity of work being performed by the party of the second part thereon, but such inspection shall be conducted in such manner as not to interfere with the work of the party of the second part.

XV.

Inspection of Books

Party of the second part hereby agrees to furnish all information including smelter returns, correspondence and bank statements which first party may require in order to assure it that it is receiving the amount of royalty or net proceeds of said property as herein provided for; second party further agrees to render to first party at Boise, Idaho, on the 20th day of each month, a statement which shall fully set forth the full particulars of the operations of the preceding month, and at the

Defendant's Exhibit No. 4—(Continued)

same time making such purchase price payments as may then be due under the terms of this agreement, and the party of the first part, at reasonable times, or at least every six months, shall have access to the books of account of party of second part relating to the operation of said property for the purpose of inspection.

XVI.

Assignment

It is further expressly agreed and covenanted that this agreement is assignable by second party, and that this agreement, and all its terms and conditions shall be binding upon the heirs, successors, and assigns of both the parties hereto; provided, however, that in the event the second party makes an assignment of this option its assignee or assignees shall, by the taking of this agreement or or assignment, assume all obligations to be performed hereunder by the second party and thereupon second party shall notify first party in writing of such assignment giving the name and address of such assignee or assignees, and from and after the receipt of such notice by first party, second party shall be relieved from all liability on account of any act or omission on his part thereafter.

XVII.

It is further stipulated and agreed that in the event the party of the second part decides that any of the claims hereinbefore described do not

Defendant's Exhibit No. 4—(Continued)
have sufficient mineral to justify the development work or the doing of the annual assessment work thereon that such claims may be abandoned whenever first party consents thereto in writing, signed by the President and Secretary of the party of first part.

XVIII.

It is hereby specifically agreed that this agreement modifies, supersedes, and takes the place of all other agreements heretofore entered into between the parties hereto relative to the above described properties and that this agreement is to be construed without reference to any of said agreements.

UNITED MERCURY MINES
COMPANY,

By J. J. OBERBILLIG,
President.

(Corporate Seal)

Attest:

J. F. KOELSCH, Secretary.

Party of First Part.

F. W. BRADLEY,

Party of the Second Part.

Defendant's Exhibit No. 4—(Continued)

Exhibit A

Payroll for Cinnabar Claim

Labor for June

Name	Total	B. H. Charge	Amt.
M. Lee	120.00	37.50	157.50
E. D. Lake	120.00	37.50	157.50
M. B. Smith.....	150.00	37.50	187.50
Geo. Fenley	75.00	37.50	112.50
Jas. Feeny	76.00	23.75	99.75
Ed McBeth	76.00	23.75	99.75
			<hr/>
			814.50

Meadow Creek Claim

Grant Drake	120.00	37.50	157.50
C. E. Kuhn	105.00	37.50	142.50
			<hr/>
			300.00

Cinnabar Claim—Labor for July

James Feeney	102.00	31.87	133.87
Geo. Cowan	38.00	11.88	49.88
			<hr/>
			183.75

Cinnabar Claim—Labor for May

M. Lee	124.00	38.75	162.75
E. D. Lake.....	64.00	17.75	81.75
M. B. Smith.....	145.00	36.25	181.25
Geo. Fenley	75.00	38.75	113.75
			<hr/>
			539.50

Meadow Creek Claim

Grant Drake	124.00	38.75	162.75
C. E. Kuhn.....	108.50	38.75	147.25
			<hr/>
			310.00

Total, 2,147.75

Defendant's Exhibit No. 4—(Continued)

Exhibit B

United Mercury Mines Company, Dr.

To

Robert Lewis Estate.....	15,000.00
H. S. Levander.....	1,000.00
Hawley & Hawley.....	4,000.00
	<hr/>
	20,000.00

EXHIBIT "B"

July 5, 1928

Crocker First Federal Trust Company,
N.W. Cor. Post and Montgomery Sts.,
San Francisco, Calif.

Re: United Mercury - Bradley Escrow. Attention: Mr. Hannon.

Gentlemen:

Under date of August 20, 1927, the United Mercury Mines Company, an Idaho corporation, gave Crocker First National Bank of San Francisco, written instructions concerning the delivery to me and my assigns of a certain deed from it to me and my assigns, deposited in escrow with said letter, upon the performance by me or my assigns of certain conditions under the provisions of a written Agreement between said Mercury Mines Company and me, dated August 5, 1927; and certain addenda to said Agreement of August 5, 1927, dated February 1, 1928, and made a part of it, were afterwards executed by said Mercury Mines Company and delivered to you; and you are holding and managing the escrow thus created.

Thereafter, pursuant to the terms of said escrow instructions, there was delivered into said escrow

Defendant's Exhibit No. 4—(Continued)

a deed of certain additional lands from said United Mercury Mines Company to me and my assigns, dated December 19, 1927.

Thereafter, pursuant to the terms of said escrow instructions, there was delivered into said escrow a deed of still other additional lands from said United Mercury Mines Company to me and my assigns, dated March 31, 1928.

I am now writing to notify you that all of my interest in and under said agreement between United Mercury Mines Company and myself, dated August 5, 1927, and in and under said addenda to said agreement added to and made a part thereof, dated February 1, 1928, has been acquired and is owned by Yellow Pine Company, a Calif. corporation, whose office address is 1022 Crocker Building, San Francisco, California, through assignments heretofore executed and caused to be executed by me; and I am herewith depositing into said escrow with you a deed of even date herewith from myself and my wife to said Yellow Pine Company, its successors and assigns, covering all three of the parcels of land set forth in said three separate deeds from said Mercury Mines Company to me, and you are instructed that the enclosed deed is delivered to you under the conditions contained in said written instructions of August 20, 1927, and is to be held in escrow by you until the payments named in the option shall have been made, or until this deed and the other deeds heretofore deposited are delivered to said Yellow Pine Company, as-

Defendant's Exhibit No. 4—(Continued)

signee, or are released, in accordance with the agreement contained in said instructions of Aug. 20, 1927.

Very sincerely,

/s/ F. W. BRADLEY.

San Francisco, California,

August 20th, 1927

Crocker First National Bank of San Francisco,
San Francisco, California.

Gentlemen:

There is handed to you herewith a deed dated August 5, 1927, from United Mercury Mines Company, an Idaho corporation, conveying to F. W. Bradley, of San Francisco, California, his heirs and assigns, certain mining property located in the Yellow Pine Mining District, Valley County, State of Idaho.

When and if said F. W. Bradley, his heirs, executors or assigns, shall hereafter pay to you the aggregate total amount of One Million Five Hundred Thousand Dollars (\$1,500,000), you will deliver the enclosed deed to said F. W. Bradley, or to his order, or his heirs, executors or assigns, or their or either of their order. All moneys so paid to you, you will immediately place to the credit of said United Mercury Mines Company in your bank, and notify it at Boise, Idaho, of said credit or credits.

When and if said F. W. Bradley, his heirs, exec-

Defendant's Exhibit No. 4—(Continued)

utors or assigns, shall at any time hereafter notify you in writing that he (or they) does not intend to proceed further under the agreement dated the 5th day of August, 1927, between said United Mercury Mines Company, party of the first part, and said F. W. Bradley, party of the second part, then you will, upon the receipt of said written notice, redeliver the said deed to the United Mercury Mines Company, or to its order.

In the event that a dispute shall hereafter arise between said United Mercury Mines Company, its successors or assigns, and said F. W. Bradley, his heirs, executors or assigns, over the delivery by you of the said deed, then and in that event you shall retain possession of the said deed until the said dispute is adjusted, or until you have been directed by final judgment of a court of competent jurisdiction with respect to the delivery thereof, and no liability of any kind or character shall attach to your Bank by reason of your failure to deliver said deed pending said dispute or the adjustment thereof, or pending litigation with respect to the delivery of said deed; provided, however, that if and when said F. W. Bradley, his heirs, executors or assigns shall have paid said sum of \$1,500,000.00, then said deed or deeds shall be delivered forthwith to him or them, anything herein to the contrary notwithstanding.

Any other deed or deeds from said United Mercury Mines Company to F. W. Bradley, which may be hereafter delivered to you, shall be held

Defendant's Exhibit No. 4—(Continued)
or delivered by you in accordance with the foregoing terms and conditions.

Very truly yours,

[Seal] UNITED MERCURY MINES
COMPANY,

By J. J. OBERBILLIG,
Its President,

By J. F. KOELSCH,
Its Secretary,

[Seal] F. W. BRADLEY,

Accepted: Crocker First National Bank of San
Francisco,

By F. G. WILLIS,
Vice President.

EXHIBIT C

Addenda to Agreement and Option Dated August
5, 1927, Between The United Mercury Mines
Company and F. W. Bradley Relating to the
Cinnabar and Meadow Creek Groups of Lode
Mining Claims.

This Agreement, Made and entered into this 1st
day of February, 1928, at San Francisco, California, by and between the United Mercury Mines
Company, a corporation organized and existing
under and by virtue of the laws of the State of
Idaho, as party of the first part, and F. W. Bradley,
of San Francisco, California, as party of the
second part, Witnesseth:

Defendant's Exhibit No. 4—(Continued)

That Whereas, the parties hereto did on or about the 5th day of August, 1927, enter into an option and agreement concerning and pertaining to the Cinnabar and Meadow Creek Groups of lode mining claims situate in Valley County, State of Idaho; and,

Whereas, in paragraph VII on pages 18 and 19 of said option agreement it was provided that the rights of second party should in certain contingencies be forfeited without demand or notice; and,

Whereas, it has been agreed by and between the parties to substitute in said option a new paragraph XII, which said paragraph shall provide for a notice to be given by first party to second party in the event it claims that said second party has failed to perform the covenants by him to be performed under said option.

Now, Therefore, for and in consideration of the premises and the continuation of development work on said claims by said second party, and in consideration of the sum of One (\$1.00) Dollar paid by the second party to the party of the first part, the receipt of which is hereby acknowledged, it is hereby stipulated and agreed as follows:

I.

That paragraph XII on pages 18 and 19 of that certain option agreement, dated the 5th day of August, 1927, shall be amended to read as follows:

Defendant's Exhibit No. 4—(Continued)

Forfeiture

"It is hereby expressly stipulated and agreed that this is an option contract and not a contract to purchase, and not a buy and sell agreement, nor a contract of or to purchase, and that time is of the essence of this contract, and that in the event the party of the second part fails to perform the conditions of this agreement strictly according to the terms hereof, or fails to keep each and every covenant by him to be kept, and fails within 60 days after the receipt of notice and demand from first party to keep and perform any covenant herein by him to be kept and performed, then in that event, all the right of the party of the second part, and his assigns, shall at the option of the party of the first part, terminate, and all the payments and improvements which shall have been made by the party of the second part, or his assigns, and all buildings erected or used as hereinbefore provided shall in such event be forfeited to the party of the first part, and that said payments and improvements shall be considered as liquidated damages, the manner of ascertaining the actual damages being difficult, provided, however, that in the event second party desires at any time to be relieved further obligation to proceed under this agreement he shall give notice in writing to that effect by United States mail, postage prepaid, or by telegram to the party of the first part or shall serve upon first party at 605 Eastman Building, Boise, Idaho, and upon the Crocker First National Bank

Defendant's Exhibit No. 4—(Continued)

of San Francisco, California, a written notice of his intention not to proceed further under this agreement, and shall, thereafter be relieved from all obligation to proceed under and from any and all liability on account of any omission thereafter, anything herein to the contrary notwithstanding; that said Crocker First National Bank of San Francisco, shall return the deed to first party herein provided for, and the same shall be null and void."

II.

It is further stipulated and agreed that except for the above and foregoing modification of said paragraph XII as contained herein, the said option agreement has not, in any particular, been modified, changed or altered.

In Witness Whereof, the parties hereto have hereunto set their hands and seals the day and year in this agreement first above written.

[Seal] UNITED MERCURY MINES
 COMPANY,
By J. J. OBERBILLIG,
 President.

Attest:

J. F. KOELSCH, Secretary.
Party of the First Part.

F. W. BRADLEY,
Party of the Second Part.

Defendant's Exhibit No. 4—(Continued)

EXHIBIT D

Modification of Agreement and Option Dated August 5, 1927, Between The United Mercury Mines Company and The Yellow Pine Company, a Corporation, Relating to the Cinnabar and Meadow Creek Groups of Lode Mining Claims.

This Agreement, Made and entered into this 30th day of August, 1929, by and between the United Mercury Mines Company, a corporation organized and existing under and by virtue of the laws of the State of Idaho, as party of the first part, and the Yellow Pine Company, a corporation organized and existing under and by virtue of the laws of the State of California and authorized to do business in the State of Idaho, as party of the second part, Witnesseth:

That Whereas, The United Mercury Mines Company, a corporation, did on or about the 5th day of August, 1927, enter into an option and agreement with F. W. Bradley, which said option agreement pertained to the Cinnabar and Meadow Creek Groups of Lode Mining Claims situate in Valley County, State of Idaho;

And Whereas, Said contract has been assigned by the said F. W. Bradley to the Yellow Pine Company, a corporation;

And Whereas, The parties desire to modify the wording in Article II and Subdivision (a) of Article V of said agreement;

Defendant's Exhibit No. 4—(Continued)

And Whereas, It has been agreed by and between the parties to substitute in said option a new Article II and a new Subdivision (a) of Article V.

Now, Therefore, For and in consideration of the premises and the continuation of the development of said claims by second party, and in consideration of the sum of One (\$1.00) Dollar, paid by the second party to the first party, the receipt of which is hereby acknowledged, it is hereby stipulated and agreed as follows, to-wit:

I.

That Article II commencing on page 6 of said option and continuing on to page 8 of said option and agreement shall be amended to read as follows:

II.

Manner of Payment:

“The purchase price for all of the interests of the party of the first part in and to said properties is to be paid by the second party by his depositing to the credit of party of first part in the Crocker First National Bank of San Francisco, California, until the purchase price of One Million Five Hundred Thousand (\$1,500,000.00) Dollars is paid; royalties from all ores, bullion, and minerals mined or taken from said claims as follows:

First: During the period from the date that production starts as hereinafter defined, and/or until second party shall have been repaid his investment in said property with interest at 8% per

Defendant's Exhibit No. 4—(Continued)

annum a royalty of 20% of the net proceeds from any and all ore from said property shipped, mined, milled or treated shall be paid by second party to said Crocker First National Bank for the credit of the first party.

Second: Whenever second party shall have been repaid his investment in said properties together with interest thereon at 8% per annum, said second party shall pay to the first party a royalty of 50% of the net proceeds from any and all ore from said property shipped, mined, milled or treated after production starts, until milled or treated after production starts, until the entire purchase price shall have been paid; said royalty to be paid by second party by his depositing the same in said Crocker First National Bank for credit of first party. It being understood and agreed by and between the parties hereto that production shall be deemed to have started whenever the party of the second part has erected and put in operation a reduction plant for handling quicksilver ore or reducing any of the ores from said properties; production shall also be deemed to have started whenever any commercial ore, bullion, metals or concentrates are taken from said properties.

Net Proceeds:

By the term 'net proceeds' as used in this instrument, is meant and intended the difference between the cash received from the sale of ore, bullion, metals or concentrates mined from or produced upon

Defendant's Exhibit No. 4—(Continued)

said properties, and the actual cash cost of producing the same; provided, however, that by the words 'actual cash cost' is meant only the actual expenses for labor, supplies, materials, fuel, power and insurance and taxes required for mining, milling or for reducing and for transportation and marketing charges. Said royalties hereinbefore described to be paid party of first part, shall be deposited to the credit of the first party in said Bank on or before the 20th day of the month next succeeding the receipt of said proceeds by second party; the same to be paid each and every month after production starts, when there are any net proceeds as defined herein.

Development May Be In Several Units:

It is understood and agreed that the said properties may be developed by second party in what is commonly called a two-stage development, and the party of the second part may proceed and build a mill of approximately 150 ton daily capacity, and at a later time build a mill or mills and other works of greater capacity and that the said second mill or mills and works in connection therewith when so constructed by said party of the second part shall be considered as a part of the investment of the party of the second part in determining whether or not under this agreement a royalty of 20% or of 50% shall be paid."

II.

That Subdivision (a) of Article V on pages 9

Defendant's Exhibit No. 4—(Continued)
and 10 of said option agreement shall be amended
to read as follows:

“(a) That he will go into the actual possession of said properties and commence bona fide development work thereon upon the signing of this agreement, and that during the year ending August 1st, 1928, and during each and every year thereafter he shall expend in developing, equipping and mining in and upon or for the benefit of said properties, the sum of at least Twenty-four Thousand (\$24,000.00) Dollars, subject to the provisions as to discontinuance and relief from the obligations to proceed further hereunder as set forth in Paragraph XII hereof, and that thereafter, during the life of this option, he shall work and develop the same with an adequate force of men for economic mining, unless prevented by Acts of God, war, invasion, labor strikes, or other circumstances, acts or conditions beyond his control.”

III.

It is further stipulated and agreed that except for the above and foregoing modification of said paragraphs as herein contained, the said option agreement has not by this instrument in any particular been amended, changed or altered; it being understood that Paragraph XII of said original option was amended by an addenda dated February 1, 1927.

In Witness Whereof, The parties hereto have

Defendant's Exhibit No. 4—(Continued)
hereunto set their hands and seals the day and year
in this agreement first above written.

[Seal] UNITED MERCURY MINES
COMPANY,

By J. J. OBERBILLIG,
President.

Attest:

J. F. KOELSCH, Secretary.
Party of the First Part.

[Seal] YELLOW PINE COMPANY,
By F. W. BRADLEY,
President.

Attest:

E. A. GRIFFEN, Secretary.
Party of the Second Part.

DEFENDANT'S EXHIBIT No. 5
(Copy)

OPTION AGREEMENT

This Agreement, Made and entered into this 16th day of May, 1939, by and between the United Mercury Mines Company, a corporation organized and existing under and by virtue of the laws of the State of Idaho, as party of the first part, hereinafter called the Optionor, and the Bradley Mining Co., a corporation organized and existing under and by virtue of the laws of the State of California and authorized to do business in the State of Idaho, the party of the second part, hereinafter called the Optionee, Witnesseth:

Defendant's Exhibit No. 5—(Continued)
Description of Claims

That Whereas, the Optionor is the owner (except as against the paramount title of the United States) of two groups of lode and placer mining claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, the first of said groups being commonly known as the Meadow Creek Group, and the second of said groups being commonly known as the Cinnabar Group, comprising lode and placer claims and comprising the following named mining claims, the notices of location of which are of record in the office of the County Recorder of Valley County, State of Idaho, at the book and page number herein stated, to-wit:

Meadow Creek

Meadow Creek No. 1—Patented Book 4, Quartz, Page 118.

Meadow Creek No. 2—Patented Book 4, Quartz, Page 118.

(Balance of description has not been copied.)

Also the mining claims, grounds and lands situate in the Yellow Pine Mining District in Valley County, State of Idaho, to-wit:

Name of Claim: Hennessy No. 1; quartz locations: Book 5, Page 157.

Name of Claim: Hennessy No. 2; quartz locations: Book 5, Page 158.

(Balance has not been copied.)

Page 6

and also all that portion of the Homestake, the

Defendant's Exhibit No. 5—(Continued)

notice of location of which is of record in the office of the County Recorder of Valley County, Idaho, in Book 5 of Quartz locations at page 350, and all that portion of the Homestake No. 2, notice of location of which is of record in the office of the County Recorder of Valley County, Idaho, in Book 5 of Quartz Locations at page 472, lying South of the line hereinafter described, all of which records are hereby referred to for a more particular description of said claims.

Together with an easement for a Tailing pond or ponds, and a right of way for a ditch conveying the waters of Sugar Creek through a by-pass, and the right to enter upon the hereinafter described lands for the purpose of diverting the waters of Sugar Creek through a by-pass and maintaining and operating a Tailing pond upon the following described lands situate in Valley County, State of Idaho, to-wit:

Said easements being in, over and upon a tract of land situate in the Yellow Pine Mining District in Valley County, Idaho, the southerly boundary of which is described (Balance of description has not been copied).

Page 7—Meadow Creek Group

Optionee to have the right to build a dam or dams, a road or roads, the right to ingress to and egress from said lands, and the whole thereof, and to flood and deposit tailings upon said lands, and the whole thereof; provided, however, that if Op-

Defendant's Exhibit No. 5—(Continued)

tionee floods or destroys the present road which is along the north side of Sugar Creek, Optionee shall construct a new road in the place thereof, having the same passability as the present road and provided, further, that Optionee shall not dump or impound tailings on the Hennessy Extension and Homestake No. 3 lode mining claims as the same are now located on the ground; provided, further, that the Antimony Gold Ores Company, a corporation, its successors and assigns, shall have the right to dump tailings on any portion of the ground embraced in said easement; provided, further, that Optionee shall not by-pass Sugar Creek at a point northeasterly of the northeasterly end line of the Midway No. 19 lode mining claim.

Page 8

The above line used in describing the easements hereinbefore mentioned is the northerly boundary line of the said Meadow Creek Group.

Cinnabar Group

Flyer: Amended, Book 6, Quartz, Page 75.

Emerald No. 1: Original, Book 3, Quartz, Page 396.

(Balance has not been copied.)

Page 10

All of which records are hereby referred to for a more particular description of said claims.

Page 11

And Whereas, the United Mercury Mines Com-

Defendant's Exhibit No. 5—(Continued)

pany, a corporation, did on or about the 5th day of August, 1927, enter into an option agreement with F. W. Bradley of San Francisco, which said option agreement pertained to the said Cinnabar and Meadow Creek Groups of lode and placer claims situate in the Yellow Pine Mining District, Valley County, State of Idaho, said option contract having been assigned by said F. W. Bradley to the Yellow Pine Company, a corporation;

And Whereas, the party of the second part went into actual possession of said properties and began bona fide development work thereon upon the signing of and in accordance with the provisions of said option agreement dated August 5th, 1927, and has during each and every year thereafter expended in developing and equipping in, upon, and/or for the benefit of said properties a sum of not less than Twenty-four Thousand Dollars (\$24,000.00);

And Whereas, the party of the second part has in accordance with the provisions of said option agreement dated August 5th, 1927, performed the necessary annual assessment work during each and every year from the date of said option agreement;

And Whereas, the party of the second part did, upon signing and in accordance with the said option agreement dated August 5th, 1927, pay unto the said first party or for its use and benefit the sum of Two Thousand One Hundred Forty-seven and 75/100 Dollars (\$2,147.75).

And Whereas, the party of the second part did

Defendant's Exhibit No. 5—(Continued)

pay to the said first party, or for its use and benefit, the sum of Ten Thousand Dollars (\$10,000.00) on or before the first day of August, 1928, and also the sum of Ten Thousand Dollars (\$10,000.00) on or before the first day of February, 1929, in accordance with the provisions of said option agreement dated August 5th, 1927;

And Whereas, the party of the second part has in each and every other respect complied with all the terms and conditions of said option agreement dated August 5th, 1927, from the date thereof;

And Whereas, the said United Mercury Mines Company, a corporation, and the said Yellow Pine Company, a corporation, did by a supplemental agreement entitled "Addenda to Agreement and Option dated August 5th, 1927, between The United Mercury Mines Company and F. W. Bradley Relating to the Cinnabar and Meadow Creek Groups of Lode Mining Claims," and dated the first day of February, 1928, further modify and change certain parts of said option contract dated the 5th day of August, 1927;

And Whereas, the said option contract dated August 5th, 1927, was further modified and changed in certain parts by a supplemental agreement dated the 30th day of August, 1929, by and between the said United Mercury Mines Company, a corporation, and the said Yellow Pine Company, a corporation;

And Whereas, the said United Mercury Mines Company, [Page 13] a corporation, and the said

Defendant's Exhibit No. 5—(Continued)

Yellow Pine Company, a corporation, desire, each for itself, further changes, additions and modifications in and to said option agreement dated August 5th, 1927;

And Whereas, on or about the 3rd day of October 1930, the United Mercury Mines Company and the Yellow Pine Company entered into a new agreement which merged within its terms and conditions all prior agreements hereinbefore referred to;

And Whereas, subsequent to said agreement on October 3, 1930, the Yellow Pine Company and its successor in interest, the Bradley Mining Co., acquired a group of mining claims known as the Hennessy Group, which said group of claims was acquired with the understanding and agreement that it would become a part of the Meadow Creek Group of lode mining claims and to be owned by the United Mercury Mines Company until the acquisition of the entire Meadow Creek Group by the Yellow Pine Company;

And Whereas, the Bradley Mining Co. has, or upon the execution and delivery of this instrument will, deliver to the United Mercury Mines Company a deed to certain claims out of said Hennessy Group of mining claims;

And Whereas, said Yellow Pine Company has assigned all of its interests in said Meadow Creek Group of lode mining claims and all its right, title and interest in and to the option hereinbefore mentioned to the Bradley Mining Co., a corporation;

Defendant's Exhibit No. 5—(Continued)

Page 14

And Whereas, the said United Mercury Mining Company, a corporation, and the said Bradley Mining Co., a corporation, further desire to enter into a new option agreement, which said agreement shall finally express the understanding and agreement between the parties hereto;

And Whereas, the Optionor is willing to give to the Optionee an option to purchase the two groups of claims above described under the terms and conditions herein contained, and the Optionee is willing to take an option to purchase said groups of mining claims under the terms and conditions herein expressed;

Now, Therefore, for and in consideration of the premises and the mutual covenants herein contained, and for the sum of Five Hundred Fifty-one and 46/100 Dollars (\$551.46) paid by the Optionee to the Optionor, the receipt whereof by the Optionor is hereby acknowledged, it is mutually covenanted, agreed and understood by and between the parties hereto as follows, to-wit:

I.

Merger of Negotiations

It is hereby specifically understood and agreed that this instrument of option contract and agreement rescinds, nullifies, supersedes, and takes and place of all other contracts and agreements of every kind and character between the parties hereto and between the Optionor and Fred W. Bradley and the

Defendant's Exhibit No. 5—(Continued)

Yellow Pine Mining Company, and that all such prior contracts and all negotiations [Page 15] between the parties hereto relative to the hereinbefore described properties, whether written or oral, of any kind or character, are merged herein, and that this agreement is to be construed without reference to any of said former agreements or negotiations.

II.

Severable Options

It is understood and agreed by and between the parties hereto, as between the parties hereto, their successors and assigns, that severable options are herein given by the Optionor to the Optionee for the two groups of mining claims hereinbefore described, and that the Optionee may elect to take and pay for the said Meadow Creek Group of mining claims as hereinbefore described without being compelled to take and pay for the said Cinnabar Group.

III.

Options Given

The said Optionor does hereby grant and accord unto the Optionee the sole and exclusive right, privilege and option to purchase all the right, title and interest of the Optionor in and to the following:

(a) Said Meadow Creek Group of lode mining claims and the said Cinnabar Group of lode mining claims hereinbefore described;

(b) Together with all dips, spurs and angles of all lodes located therein;

Defendant's Exhibit No. 5—(Continued)

(c) Together with all other mining claims now owned by or that may hereafter be located or acquired by said Optionor during the life of this agreement within 1500 linear feet of the extreme exterior boundaries of said [Page 16] Meadow Creek and Cinnabar Groups of lode mining claims, or within, or adjacent, or contiguous thereto;

(d) Together with the tenements, hereditaments and appurtenances and rights and privileges thereunto belonging or in anywise appertaining;

(e) Together with the personal property belonging to said Optionor situate upon said mining claims;

(f) Together with all millsites, water rights, tail races, tailing sites, and tailing dams or easements that are now owned or may in the future be acquired by said Optionor for use in connection with said claims, or any of them.

The purchase price for said Meadow Creek Group of lode mining claims to be the sum of Nine Hundred Thousand Dollars (\$900,000.00), lawful money of the United States of America, said sum to be paid (subject to the right of the Optionee to discontinue this agreement and to be relieved from further obligations to proceed hereunder as set forth in Paragraph XV hereof) at the times and in the manner hereinafter provided, the said option to be subject at all times to the terms, conditions and provisions hereinafter expressed.

Defendant's Exhibit No. 5—(Continued)

Purchase Price

The purchase price for the Cinnabar Group of lode mining claims shall be the sum of Six Hundred Thousand Dollars (\$600,000.00), lawful money of the United States of America, in addition to the \$900,000.00 for the Meadow Creek Group, said sum to be paid (subject to the right of the Optionee to discontinue this agreement and [Page 17] to be relieved from further obligations to proceed hereunder as set forth in Paragraph XV hereof) at the times and in the manner hereinafter provided, the said option to be subject at all times to the terms, conditions and provisions hereinafter expressed.

IV.

The said Optionor does hereby give, grant and accord unto the Optionee, or its representative or representatives, the sole and exclusive option, privilege and right to enter in and upon and to continue with the actual possession of said mining claims and work in and on them for the purpose of developing, equipping, and extracting ores or metals or values from said claims, and in the manner and to the extent and at such places as may, in the judgment of said optionee, be best suited to the best interests of both parties hereto; said option, however, to be subject at all times to the terms, covenants and provisions hereinafter expressed.

V.

Development Work

The Optionee hereby agrees, in the event it con-

Defendant's Exhibit No. 5—(Continued)

tinues to exercise its rights under this option, to do and perform (subject always to the right of the Optionee to discontinue this agreement and to be relieved from any further obligation to proceed hereunder as set forth in Paragraph XV hereof) the following:

(a) To perform and complete upon, or in or for the benefit of said Meadow Creek Group of mining claims, prior to the first day of May of each and every year that said Optionee remains in or is entitled to the possession [Page 18] of said Meadow Creek Group under the terms of this agreement, the necessary annual assessment work to hold and protect said claims under the mining laws of the United States and the State of Idaho, and to file and record, on or before the first day of June of each and every year during the occupation of said premises by said Optionee under the provisions of this agreement, in the office of the County Recorder of Valley County, State of Idaho, on behalf of Optionor, the necessary proofs of such annual labor or assessment work upon said Meadow Creek Group of mining claims. Optionee agrees to file proofs of annual assessment work for said Cinnabar Group insofar as the work done on the Meadow Creek Group is applicable thereto, the Optionee to have the discretion in determining what work is applicable to said Cinnabar Group.

(b) To spend in, upon, and for the benefit of or on account of said properties, annually during the life of this agreement, the sum of at least Twenty

Defendant's Exhibit No. 5—(Continued)

Five Thousand Dollars (\$25,000.00), said sum to include, but not necessarily in addition to, such sums required for the annual assessment work provided in sub-paragraph (a) immediately preceding, it being understood that the places where and the manner in which the said sum shall be expended shall be in the sole discretion of the Optionee, and that if said sum spent can be applied as assessment work on said claims it shall not be necessary for Optionee to perform other or additional assessment work.

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(c) To pay to the Optionor, at the times and in the manner hereinafter provided, the following royalties upon all ores, metals or values extracted from the mining grounds included in this option during the periods hereinafter named;

First: For the period from August 1st, 1939, and ending at midnight, July 31st, 1944, a royalty of seven and one-half per cent ($7\frac{1}{2}\%$) upon all net smelter, or mint returns, or net revenues, as defined herein, on all concentrates, metals, ores and values extracted from said optioned mining claims;

Second: For the period beginning August 1st, 1944, and ending at midnight, July 31st, 1949, a royalty of ten per cent (10%) upon all net smelter, or mint returns, or net revenues as defined herein on all concentrates, metals, ores and values extracted from said optioned mining claims;

Third: For the period beginning August 1st,

Defendant's Exhibit No. 5—(Continued)

1949, and thereafter, a royalty of twelve and one-half per cent ($12\frac{1}{2}\%$) upon all net smelter, or mint returns, or net revenues, as defined herein, on all concentrates, metals, ores and values extracted from said optioned mining claims.

Manner of Payment

The said royalties shall be deposited by Optionee in the Crocker First National Bank of San Francisco, California, to and for the credit and order of said Optionor, on or before the twentieth (20th) day of the calendar month next succeeding the receipt of said net [Page 20] returns by Optionee, and the same to be so paid each and every month when there are any net smelter or mint or other returns until the purchase price of said mining claims and properties has been completed as herein provided. It is agreed that concentrates cannot be hauled from the property during the late fall, winter and early spring months, and that the time when the same shall be shipped during the summer months shall be determined by Optionee. It is understood, however, that should local reduction of the concentrates become practicable as determined by the Optionee, that no concentrates will be shipped.

Certain Terms Defined

By net smelter returns, as used herein, is meant the amount received from the smelter from any ores, concentrates, metals, or values shipped to a smelter, it being understood that the smelter will

Defendant's Exhibit No. 5—(Continued)

deduct its normal smelting charges, and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped less marketing and shipping costs from Cascade, Idaho.

By net mint returns, as used herein, is meant the amount paid by any United States Mint, branch or agency thereof, less all shipping and marketing costs from Cascade, Idaho.

It is agreed that in addition to the deduction of railroad freight from Cascade, Idaho, to the smelter, [Page 21] that Optionee shall also be allowed to deduct from the net smelter returns Two dollars and Fifty Cents (\$2.50) per ton for each ton of concentrates, ores, metals or values hauled from the above described property, the said sum to be deducted from the net smelter returns before net royalty herein provided for is computed. It is also agreed that in the event that concentrates are shipped by truck to a smelter, there shall be deducted from net smelter returns the amount for trucking that it would have cost to ship the same by railroad from Cascade, Idaho, to the smelter to which the same are trucked.

It is understood and agreed that when the sum of Nine Hundred Thousand Dollars (\$900,000.00) shall have been paid by the Optionee to the Optionor then, and in that event, the escrow holders herein named shall deliver to the Optionee the

Defendant's Exhibit No. 5—(Continued)
deeds and title papers deposited with said escrow holder under the terms hereof for the above and foregoing described Meadow Creek Group.

(d) The Optionee will not remove any building or other like structure now situate upon or used in connection with the hereinbefore described properties, and it will keep the same in good condition and repair it at its own expense, and the Optionee also agrees that all improvements made and buildings placed upon said premises shall be appurtenant thereto, and in the event that the Optionee does not complete the purchase of said mining properties under the terms of this agreement, and in case [Page 22] of termination, cancellation or forfeiture hereof or hereunder, the said improvements and buildings shall become the property of the Optionor, provided, the Optionee may remove severable machinery, such as ball mills, flotation cells, generators, motors, roasters, transformers, transmission lines, and compressors, and supplies installed or placed upon said property by said Optionee or its predecessors since 1927.

No Liens Allowable

(e) The Optionee will keep the properties, and the whole thereof, free and clear of all liens of whatsoever kind or character, and the Optionee hereby covenants for itself, and its successors and assigns, to hold the Optionor harmless from any and all liens and claims of whatsoever kind or nature for wages or supplies, or any indebtedness

Defendant's Exhibit No. 5—(Continued)

whatsoever created by Optionee by reason of its possession of or its working of said claims. The Optionee shall not be deemed or considered the agent of said Optionor under the provisions of the statutes of Idaho relating to liens, or otherwise, except for the performance by Optionee of said annual assessment work.

Notices to Be Posted

(f) The Optionee will make the necessary affidavits and post and record the necessary notices to comply with the provisions of Sections 43-401 to 43-403, Idaho Code Annotated, 1932 Official Edition, so as to notify all persons that the operations to be carried on under this agreement shall be at the sole cost and expense of the Optionee, and that the Optionor shall not be responsible [Page 23] or liable in any way for the debts and obligations of the Optionee, and that contracts for labor, supplies and materials by the Optionee shall not bind the Optionor or the hereinbefore described mining properties, or any part thereof, and that full compliance with the statutes of the State of Idaho in regard to the making and filing and recording of the notices to effectuate this purpose shall be had immediately upon the execution of this agreement.

Work In Miner Like Manner

(g) To perform all work done upon said Meadow Creek Group of mining claims during the existence of this agreement in a proper and miner-like man-

Defendant's Exhibit No. 5—(Continued)

ner, and that all reasonable efforts shall be made by Optionee to keep up and work all stakes and monuments.

Taxes

(h) To pay, prior to delinquency, all taxes of every kind and character that may be levied or assessed against said property during the life of this agreement; provided, however, that if in the future a bullion or severance tax is levied or imposed, Optionee shall not be obligated to pay the same on the royalty share to which the Optionor is entitled.

(i) Optionee agrees that it will proceed, as soon as practicable, to enlarge the present mill situate on said Meadow Creek Group to a capacity of approximately three hundred (300) tons per day, the exact time of the completion of said enlargement to be left to the discretion of Optionee.

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VI.

The said Optionor does hereby covenant and agree with the said Optionee to do and perform the following things concurrently with the execution of this agreement, to-wit:

Deed In Escrow

(a) To execute a good and sufficient deed or deeds, granting and conveying to Optionee all the right, title and interest of the said Optionor in and to the Meadow Creek Group as hereinbefore described, and the whole thereof (except as against the

Defendant's Exhibit No. 5—(Continued)

paramount title of the United States of America), together with the buildings and improvements situate in or upon or appertaining to said Meadow Creek Group of mining claims, and to deposit the same in escrow with the Crocker First National Bank of San Francisco, California, with appropriate instructions to said bank to deliver said deed or deeds to the said Optionee upon the performance by it of all the terms and conditions of this agreement and the payment in full as herein provided of the sum of Nine Hundred Thousand Dollars (\$900,000.00).

(b) To execute a good and sufficient deed or deeds, granting and conveying to the said Optionee all the right, title and interest of the said Optionor in and to said Cinnabar Group of lode mining claims as hereinbefore described, and the whole thereof (except as against the paramount title of United States of America), together with the improvements and buildings situate in or upon or appertaining to said Cinnabar Group of mining claims, and to deposit in escrow with the [Page 25] Crocker First National Bank of San Francisco, California, the said deed or deeds, with appropriate instructions to said bank to deliver said deed or deeds for said Cinnabar Group to the Optionee upon the performance by it of all the terms and conditions of this agreement and the payment in full therefor by said Optionee of the sum of Six Hundred Thousand Dollars (\$600,000.00), the same to be in addition to the sum of Nine Hundred Thousand

Defendant's Exhibit No. 5—(Continued)
Dollars (\$900,000.00) herein provided for as the purchase price for the said Meadow Creek Group.

(c) To execute and acknowledge such statement or statements as may be desired by the said Optionee to be recorded in the office of the County Recorder of Valley County, Idaho, showing the giving of the hereinbefore described options.

VII.

The said Optionor does further covenant and agree, to-wit:

(a) Upon the demand of the Optionee to make and execute and place in escrow with the said Crocker First National Bank of San Francisco, California, any further deeds, instruments, conveyances or writings of whatsoever character that may be required by said Optionee in order to convey all the right, title and interest of said Optionor in and to said groups of claims and any and all claims that may hereafter be purchased or located by the Optionor within the exterior boundaries of said [Page 26] Meadow Creek Group or within the exterior boundaries of said Cinnabar Group, or within 1500 feet of the exterior limits thereof, including all appurtenances as are enumerated in subdivisions (b) to (f) inclusive, of paragraph III hereof.

VIII.

It is further stipulated and agreed by and between the parties hereto that the purchase price for said Meadow Creek Group shall be the sum of

Defendant's Exhibit No. 5—(Continued)

Nine Hundred Thousand Dollars (\$900,000.00) and the purchase price for said Cinnabar Group shall be the sum of Six Hundred Thousand Dollars (\$600,000.00).

IX.

Payment a Condition Precedent to Delivery

It is further stipulated and agreed that the payment of said purchase price is a condition precedent to the delivery of any deed or deeds for said properties, and that the deed or deeds for the mining claims and properties shall be delivered to the Optionee upon the payment to the Optionor as follows:

(a) That the deed or deeds for said Meadow Creek Group shall be delivered when Optionee shall have paid to the Optionor the sum of Nine Hundred Thousand Dollars (\$900,000.00);

(b) That the deed or deeds for the said Cinnabar Group shall be delivered to the Optionee when the total purchase price of Nine Hundred Thousand Dollars (\$900,000.00) for the Meadow Creek Group and Six Hundred [Page 27] Thousand Dollars (\$600,000.00) for the Cinnabar Group, amounting to a total purchase price of One Million Five Hundred Thousand Dollars (\$1,500,000.00) shall be paid to the Optionor as herein provided.

X.

It is further stipulated and agreed that all royalties herein provided for shall be applied and con-

Defendant's Exhibit No. 5—(Continued)
stitute a part payment of the purchase price herein provided for.

XI.

Abstracts

It is further stipulated and agreed that within ninety (90) days after written demand therefor by the Optionee made on the Optionor, the Optionor shall deliver to the Crocker First National Bank of San Francisco, California, for delivery to Optionee, or its assigns, abstracts of title for the above described Meadow Creek Group. It is agreed that the Optionee, or its assigns, shall have a period of ninety (90) days after said abstracts are delivered to said Crocker First National Bank for the examination of said abstracts of title and at or before the end of said ninety (90) days shall deliver to Optionor a written opinion containing all material objections that the said Optionee may raise to the title (except the paramount right of the United States) of the Optionor to said claims, and the Optionor shall have ninety (90) days within which to correct such material defects in said possessory right, unless, in order to correct such defects it is necessary to bring suit or [Page 28] suits to quiet title, in which event a reasonable time shall be allowed the Optionor therefor, it being understood that the corrections of such defects are not conditions precedent or dependent conditions to the making of the payments and the performance of the conditions herein by the Optionee to be kept and performed.

Defendant's Exhibit No. 5—(Continued)

In the event Optionee shall fail to deliver written objections as and within the time aforesaid, or if Optionor shall make corrections as aforesaid, the Optionee, or its assigns, shall be conclusively held to have accepted and approved such title as Optionor has agreed to convey upon the performance of this option by Optionee.

XII.

New Claims

It is agreed that Optionor at all times during the existence of this contract shall have free access to the above described properties for the purpose of inspecting said properties and making surveys, setting stakes and amending and making locations; that all amended locations made, as well as all locations or purchases of new claims and of fractional claims, within or upon the lands embraced in or within fifteen hundred (1500) feet of the general exterior lines of the general groups of claims above or within described, and all purchases and locations of mill sites, power plants, sites and water rights made either by Optionor or Optionee, or its assigns, prior to delivery of conveyance hereunder, shall be made in the name of and for the Optionor, and that all such new and amended locations shall be deemed and considered as included in this option and as part of the property to be conveyed to Optionee and no additional price shall be paid therefor, in case the payments hereinbefore described are made at the time and at the place and

Defendant's Exhibit No. 5—(Continued)
in the manner herein described. The Optionor agrees that, upon the written demand of the Optionee, it will make and execute and place in escrow in said Crocker First National Bank of San Francisco, California, a deed or deeds covering and conveying all of said new locations and filings to the Optionee, to be held by said bank subject to the terms and conditions of this option.

XIII.

Patents

The Optionor agrees that upon the written demand of the Optionee it will, in its own name, apply for a United States Patent or Patents for the above described mining claims, or any part thereof, the same to be secured, however, at the expense of the Optionee.

XIV.

Modification In Writing. Waivers

It is further stipulated and agreed that no modification shall be of any force or effect or binding upon either or any of the parties hereto unless made in writing and signed by both parties hereto; and that the waiver by Optionor of any breach of any one or more covenants shall not be construed as a waiver of the breach of any covenant, nor of time as of the essence hereof.

Page 30

XV.

Forfeiture

It is expressly stipulated and agreed that this is

Defendant's Exhibit No. 5—(Continued)

an option contract and not a contract of purchase, and not a buy and sell agreement, nor a contract of or to purchase, and that time is of the essence of this contract, and that in the event the Optionee fails to perform the conditions of this agreement strictly according to the terms hereof, or fails to keep each and every covenant by it to be kept, and fails within sixty (60) days after the receipt of written notice and demand from Optionor, sent by registered mail to Optionee, addressed to it at 922 Crocker Building, San Francisco, California, to keep and perform any covenant herein by it to be kept and performed, then, and in that event, all the right of the Optionee, and its assigns, shall at the option of the Optionor terminate, and all the payments and improvements which shall have been made by the Optionee, or its assigns, and all buildings erected or used as hereinbefore provided, shall in such event be forfeited to the Optionor, and that said payments and improvements shall be considered as liquidated damages, the manner of ascertaining the actual damages being difficult, and it is agreed that forfeiture as herein provided and the right to sue for the recovery of royalties shall be the sole remedies of the Optionor, provided, however, that in the event Optionee desires at any time to be relieved from further obligation to proceed under this agreement it shall give notice in writing to that effect by registered United States mail, to the Optionor, [Page 31] or shall serve upon Optionor at 258 Sonna Building, Boise, Idaho, and

Defendant's Exhibit No. 5—(Continued)
also registering a copy thereof to Hawley & Worthwine, 610 Eastman Building, Boise, Idaho, and upon the Crocker First National Bank of San Francisco, California, a written notice of its intention not to proceed further under this agreement, and shall thereafter be relieved from all obligation to proceed hereunder, and from any and all liability on account of any omission thereafter, anything to the contrary herein notwithstanding; that said Crocker First National Bank of San Francisco shall return the deed to Optionor herein provided for, and the same shall be null and void.

XVI.

Surrender of Possession

It is further stipulated and agreed that upon the failure of the Optionee to perform any terms or conditions of this contract within sixty (60) days after notice so to do as herein provided, it will, upon the demand of the Optionor, at once surrender said premises to the Optionor.

XVII.

Inspection of Claims and Work

It is specifically agreed that during the existence of this contract, and during the time the Optionee shall have the right to the possession of said property under this contract, the Optionor, its agents and representatives, shall have at all reasonable times free access to [Page 32] said property, and the whole thereof, for the purpose of inspecting the

Defendant's Exhibit No. 5—(Continued)

nature, character and quantity of work being performed by the Optionee thereon, but such inspection shall be conducted in such manner as not to interfere with the work of the Optionee.

XVIII.

Inspection of Books

The Optionee hereby agrees to furnish all information, including smelter returns, correspondence and bank statements, which Optionor may require in order to assure it that it is receiving the amount of royalty or net proceeds of said property as herein provided for. Optionee further agrees to render to Optionor at Boise, Idaho, on or before the 25th day of each month, a statement which will fully set forth the estimate of net smelter returns of the preceding month, and at the same time making such purchase price payments as may then be due under the terms of this agreement, and the Optionor, at reasonable times, or at least every six months, shall have access to the books of account of the Optionee relating to the operation of said property for the purpose of inspection.

XIX.

Assignment

It is further expressly agreed and covenanted that this agreement is assignable by Optionee, and that this agreement and all its terms and conditions shall be binding upon the heirs, successors and assigns of both the parties hereto; provided, however,

Defendant's Exhibit No. 5—(Continued)
that in the event the Optionee makes an assignment of this option, its assignee or assignees shall, by the taking of this agreement or [Page 33] assignment, assume all obligations to be performed hereunder by the Optionee, and thereupon the Optionee shall notify the Optionor in writing of such assignment, giving the name of such assignee or assignees, and from and after the receipt of such notice by the Optionor, Optionee shall be relieved from all liability on account of any act or omission on its part thereafter.

XX.

It is further stipulated and agreed that in the event the Optionee decides that any of the claims hereinbefore described do not have sufficient mineral to justify the development work or the doing of the annual assessment work thereon that such claims may be abandoned whenever Optionor consents thereto in writing, signed by the President and Secretary of the Optionor.

XXI.

It is understood and agreed that said Optionor shall have the right to withdraw said Cinnabar Group of lode mining claims from the terms of this option, provided the Optionee has not given prior written notice to Optionor that it desires to mine or buy said Cinnabar Group, the said written notice of its desire to withdraw said mining claims from the terms of this option to be given by Optionor by registering the same to the Optionee at 922 Crocker

Defendant's Exhibit No. 5—(Continued)

Building, San Francisco, California, and that after the giving of said written notice, then, and in [Page 34] that event, the said Optionee shall not have the right to the possession of said Cinnabar Group and the said Optionee shall be under no obligation to pay said sum of \$600,000.00 herein mentioned as the purchase price for said Cinnabar Group. If, however, the said Optionee gives prior written notice to the said Optionor of its desire to mine or buy said Cinnabar Group, said written notice to be given by registering the notice thereof to the Optionor at 258 Sonna Building, Boise, Idaho, and also registering a copy thereof to Hawley & Worthwine, 601 Eastman Building, Boise, Idaho, then, and in that event, the said Optionor shall not have the right to withdraw from the terms of this option said Cinnabar Group until the said Optionee shall, by written notice mailed as aforesaid, have given notice that it does not desire to proceed further under the option herein contained to purchase the said Cinnabar Group of lode mining claims; provided, however, that when \$900,000.00 shall have been paid under this entire option then the Optionee must, at the completion of the payment of said \$900,000.00, elect by written notice given Optionor as aforesaid, as to whether it shall continue under this option as to said Cinnabar Group; and if it does not so elect then the option herein given on said Cinnabar Group shall cease and terminate. In the event Optionee does elect to continue this option on said Cinnabar Group the

Defendant's Exhibit No. 5—(Continued)

royalties on all ores mined from either the Meadow Creek Group or the Cinnabar Group shall apply first on the purchase price of [Page 35] said Meadow Creek Group until \$900,000.00 shall have been paid, and then on the purchase price of \$600,000.00 for said Cinnabar Group, all royalties to be as prescribed herein.

In the event Optionee gives notice that it desires to mine or buy said Cinnabar Group it agrees to expend such an amount and do such work thereon, or for its benefit, as will fulfill the requirements of annual assessment work, during any period that its election to mine or buy is in force as herein provided.

XXII.

It is hereby stipulated and agreed that this agreement settles and adjusts all claims of every kind and character which the Optionor has against F. W. Bradley, the F. W. Bradley Estate, the Yellow Pine Company and The Bradley Mining Co., on account of any alleged non-performance by the said F. W. Bradley; the said Yellow Pine Company, and/or the said Bradley Mining Co., except Optionee shall account to Optionor for Optionor's percentage of the net profit on concentrates on the above described Meadow Creek property on August 1, 1939, as determined under a contract of October 3, 1930, between Optionor and the Yellow Pine Company.

XXIII.

It is hereby stipulated and agreed, and the said

Defendant's Exhibit No. 5—(Continued)

escrow holder is hereby instructed to return and deliver to the Optionor all deeds heretofore executed by the Optionor [Page 36] to F. W. Bradley, the Yellow Pine Mining Company, and/or the Bradley Mining Co., which are now filed in escrow with the above escrow holder, except that the said escrow holder shall deliver to the Optionee that certain quit claim deed, dated on or about the 31st day of March, 1937, the said quit claim deed being from the Yellow Pine Company, a corporation, to the United Mercury Mines Company, a corporation, which said deed is now on deposit in the above referred to escrow with the said escrow holder.

XXIV.

The blocked marginal captions herein contained are for convenience only and are not to be considered in construing this instrument.

UNITED MERCURY MINES
COMPANY, a corporation,

[Seal] /s/ By J. J. OBERBILLIG,
Its President
Optionor

Attest: /s/ D. D. Oberbillig, Its Asst. Secretary.

BRADLEY MINING CO.,
a corporation,

/s/ By JOHN D. BRADLEY,
Its Vice-President
Optionee

Attest: E. A. Griffen, Its Secretary.

Defendant's Exhibit No. 5—(Continued)

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State of Idaho,

County of Ada—ss.

On this 24th day of May, 1939, before me, Walter G. Bell, a Notary Public in and for said County and State, personally appeared J. J. Oberbillig and D. D. Oberbillig, known to me to be the President and Assistant Secretary, respectively, of the United Mercury Mines Company, one of the corporations that executed the above and foregoing instrument, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and official seal the day and year last above written.

[Seal] /s/ WALTER G. BELL,
Notary Public for Idaho

State of California,

City and County of San Francisco—ss.

On this 16th day of May, 1939, before me, W. W. Healey, a Notary Public in and for said County and State, personally appeared John D. Bradley and E. A. Griffen, known to me to be the Vice-President and Secretary, respectively, of the Bradley Mining Co., one of the corporations that executed the above and foregoing instrument, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my



MAR 20 1957

Addition

V.

The optionee hereby agrees, in the event it continues to exercise its rights under this option, to do and perform (subject always to the right of the optionee to discontinue this agreement and to be relieved from any further obligation to proceed hereunder as set in Paragraph ____ hereof) the following:

(a) To perform and complete upon, or in or for the benefit of said ~~two~~ ^{Walter Clark} Group(s) of mining claims, prior to the first day of May of each and every year that said optionee remains in or is entitled to the possession of ~~the property~~ ^{the said property} under the terms of this agreement, the necessary annual assessment work to hold and protect

said claims under the mining laws of the United States and the State of Idaho, and to file and record, on or before the first day of June of each and every year during the occupation of said premises by said optionee under the provisions of this agreement, in the office of the County Recorder of Valley County, State of Idaho, on behalf of optioner, the necessary proofs of such ^{the said Group(s) of} annual labor or assessment work upon said mining claims. ^X

(b) To spend in, upon, and for the benefit or on account of said properties, annually during the life of this agreement, the sum of at least twenty five

thousand Dollars (25,000.00),

said sum to include, but not necessarily in addition to, such sums required for the annual assessment work provided in sub-paragraph (a) immediately preceding, it being understood that the places where and the manner in which the said sum shall be expended shall be in the sole discretion of the optionee, and that if said sum

S.

Optionee agrees to file the proofs of annual assessment work for said American Group in no later than the date of the annual assessment for the said Group. For as the work done is approximate then to.

Development :
work :

is spent in development work that can be applied as

assessment work on said claims it shall not be necessary for optionee to perform other or additional assessment work.

(c) To pay to the optionee, at the times and in the manner hereinafter provided, the following royalties upon all ores, metals or values extracted from the mining grounds included in this option during the periods hereinafter named:

First: For the period from the date hereof and ending ~~December 31, 1943~~ ^{May 1, 1939}, a royalty of seven and one-half per cent ($7\frac{1}{2}\%$) upon all net smelter, ~~mint~~ ^{or} ~~turns~~ ^{or other net returns as defined herein} on all ~~metals~~ ^{ores} and values extracted from said optioned mining claims;

Second: For the period beginning ~~at midnight, January 1, 1944~~ ^{May 1, 1949}, and ending ~~December 31, 1949~~, a royalty of ten per cent (10%) upon all net smelter, mill or mint returns on all metals, ores and values extracted from said optioned mining claims;

Third: For the period beginning ~~January 1, 1949~~ ^{May 1, 1949}, and ~~thereafter~~, a royalty of twelve and one-half per cent ($12\frac{1}{2}\%$) upon all net smelter, ~~mint~~ or mint returns on all metals, ores and values extracted from said optioned mining claims.

The said royalties shall be deposited by optionee in the Crocker First National Bank of San Francisco, California, to and for the credit and order of said optionor, on or before the twentieth (20th) day of the calendar month next succeeding the receipt of said net returns by optionee, and the same to be so paid each and

Manner
of
Payment



every month when there are any net smelter, ~~mint~~ or mint returns until the purchase price of said mining claims and properties has been completed as herein provided.

By net smelter returns, as used herein, is meant the ~~net~~ amount received ^{from the smelter} from any ores, concentrates, metals, or values shipped to a smelter, it being understood that the smelter will deduct its ^{now} smelting charges and also may deduct charges for railroad freight from Cascade, Idaho, to said smelter ~~shall also be deducted~~.

By net ~~mint~~ returns, as used herein, is meant the net amount paid by any ~~milling~~ company, with the right of said ~~milling~~ company to deduct milling charges only.

By net ~~mint~~ returns, as used herein, is meant the ~~net~~ amount paid by any United States Mint ^{wherein (including all other United States Mints)} ~~it is understood and agreed that when the sum of~~

Nine Hundred Thousand Dollars (\$900,000.00) shall have been paid by the optionee to the optionor then, and in that event, the escrow holder herein named shall deliver to the optionee the deeds and title papers deposited with said escrow holder under the terms hereof for the above and foregoing described Meadow Creek Group.

(a) The optionee will not remove any ~~machinery~~, ^{buildings} building or other ~~equipment~~ now situate upon or used in connection with the hereinbefore described properties, and it will keep the same in good condition and repair it at its own expense, and the optionee also agrees that all improvements made and buildings placed upon said premises shall be appurtenant thereto, and in the event that the optionee does not complete the purchase of said mining properties under the terms of this agreement and in case of termination, cancellation or forfeiture hereof or hereunder, the said improvements and buildings shall

Improvements :
Not :
Severable :



the name of such assignee or assignees, and from and after the receipt of such notice by the optionor, optionee shall be relieved from all liability on account of any act or omission on its part thereafter.

XVI.

It is further stipulated and agreed that in the event the optionee decides that any of the claims hereinbefore described do not have sufficient mineral to justify the development work or the doing of the annual assessment work thereon that such claims may be abandoned whenever optionor consents thereto in writing, signed by the President and Secretary of the optionor.

XVII.

It is understood and agreed ~~that~~ in regard to the said Cinnabar Group of lode mining claims ~~hereinafter de-~~

~~scribed, that if at any time before the optionee herein~~

~~gives written notice to the optionor that it desires to~~
~~withdraw said Cinnabar Group, then said optionor shall have~~

~~the right to withdraw said group of lode mining claims~~

~~from the terms of this option, the said written notice of~~

~~its desire to withdraw said mining claims from the terms~~

~~of this option to be given by optionor by registering the~~

~~same to the optionee at 922 Crocker Building, San~~

~~Francisco, California, and that after the giving of said~~

~~written notice then, in that event, the said optionee~~

~~shall not have the right to the possession of said Cinnabar~~

~~Group and the said optionee shall be under no obligation~~

~~to pay said sum of \$600,000.00 herein mentioned as the~~

~~purchase price for said Cinnabar Group. If, however, the~~

~~said optionee gives ^{prior} written notice to the said optionor~~

~~of its desire to mine ^{or sell} said Cinnabar Group, said written~~

~~notice to be given by registering the notice thereof to~~

~~the optionor at 258 Sonoma Building, Boise, Idaho, and also~~

provided the optionee has not given prior written notice to the optionor that it desires to mine or sell said Cinnabar Group.



registering a copy thereof to Hawley and Worthwine, 610 Eastman Building, Boise, Idaho, then, in that event, the said optionor shall not have the right to withdraw from the terms of this option said Cinnabar Group until the said optionee shall, by written notice mailed as aforesaid, have given notice that it does not desire to proceed further under the option herein contained to purchase the said Cinnabar Group of lode mining claims: provided, however, that when \$900,000.00 shall have been paid under this entire option then the optionee must, at the completion of the payment of said \$900,000.00, elect by written notice given optionor as aforesaid as to whether it shall continue under this option as to said Cinnabar Group; and if it does not so elect then the option herein given on said Cinnabar Group shall cease and terminate. In the event optionee does elect to continue this option on said Cinnabar Group the royalties on all ores mined from either the Meadow Creek Group or the Cinnabar Group shall apply first on the purchase price of said Meadow Creek Group until \$900,000.00 shall have been paid, and then on the purchase price of \$600,000.00 for said Cinnabar Group, all royalties to be as prescribed herein.

XXIII.

It is hereby stipulated and agreed that this agreement settles and adjusts all claims of every kind and character which the optionor has against F. W. Bradley, the F. W. Bradley Estate, the Yellow Pine Company, and the Bradley Mining Company on account of any alleged non-performance by the said F. W. Bradley, the said Yellow Pine Company, and/or the said Bradley Mining Company.

See the several optionor gives notice that it desires to mine or sell such work thereon as far as it would as well liquidate the agreement & returned agreement with during the period that it elects to mine or sell

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DEFENDANT'S EXHIBIT No. 6

AGREEMENT

This Agreement, Made and entered into this 20th day of July, 1950, by and between the United Mercury Mines Company, an Idaho corporation, with its principal place of business at Boise, Idaho, and Oscar W. Worthwine, of Boise, Idaho, parties of the first part, and the Bradley Mining Co., a corporation organized and existing under and by virtue of the laws of the State of California, and authorized to do business in the State of Idaho by virtue of a full and complete compliance with the Constitution and laws of the State of Idaho, party of the second part,

Witnesseth:

Whereas, the United Mercury Mines Company did, by a Conveyance and Royalty Agreement dated the 31st day of December, 1941, and recorded in the office of the County Recorder of Valley County, Idaho at 9:01 a.m., on the 30th day of January, 1942, in Book 20 of Deeds at page 510 thereof, convey to the Bradley Mining Co., the Meadow Creek Group of Mining Claims situate in the Yellow Pine Mining District in Valley County, Idaho; and

Whereas, by said Conveyance and Royalty Agreement it was agreed by and between the parties that the said Bradley Mining Co. would pay to the United Mercury Mines Company a royalty, all as set forth in said Conveyance and Royalty Agreement, and that out of the royalty due to the said United Mercury Mines Company, the said Bradley

Defendant's Exhibit No. 6—(Continued)

Mining Co. would pay direct to Oscar W. Worthwine three and one-third ($3\frac{1}{3}\%$) percent of the royalty due to the said United Mercury Mines Company; and

Whereas, various other properties have been conveyed to the Bradley Mining Co. by the United Mercury Mines Company under the terms and conditions set forth in the above described Conveyance and Royalty Agreement; and

Whereas, under the terms and conditions of said Conveyance and Royalty Agreement the said Bradley Mining Co. is obligated to pay a monthly royalty as above set out, said monthly royalty to be paid on or before the 20th day of the month next succeeding the receipt by said Bradley Mining Co. of moneys received during the previous month; and

Whereas, the said Bradley Mining Co., did, on the 20th day of June, 1950, pay to the United Mercury Mines Company and said Oscar W. Worthwine the royalties due for the month of May, 1950; and

Whereas, the parties hereto desire to postpone for one (1) year the payment of royalties accruing to said United Mercury Mines Company and Oscar W. Worthwine for the months of June to November, 1950, both inclusive;

Now, Therefore, for and in consideration of the premises and the mutual covenants herein contained, it is hereby agreed:

(1) That the royalty becoming due and payable under the above described Conveyance and Royalty

Defendant's Exhibit No. 6—(Continued)

Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of June, 1950, which would become due July 20, 1950, shall be postponed until July 20, 1951, at which time the said Bradley Mining Co. shall pay the same;

That the royalty becoming due and payable under the above described Conveyance and Royalty Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of July, 1950, which would become due August 20, 1950, shall be postponed until August 20, 1951, at which time the said Bradley Mining Co. shall pay the same;

That the royalty becoming due and payable under the above described Conveyance and Royalty Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of August, 1950, which would become due September 20, 1950, shall be postponed until September 20, 1951, at which time the said Bradley Mining Co. shall pay the same;

That the royalty becoming due and payable under the above described Conveyance and Royalty Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of September, 1950, which would become due October 20, 1950, shall be postponed until October 20, 1951, at which time the said Bradley Mining Co. shall pay the same;

That the royalty becoming due and payable under

Defendant's Exhibit No. 6—(Continued)

the above described Conveyance and Royalty Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of October, 1950, which would become due November 20, 1950, shall be postponed until November 20, 1951, at which time the said Bradley Mining Co. shall pay the same;

That the royalty becoming due and payable under the above described Conveyance and Royalty Agreement by the Bradley Mining Co. to the United Mercury Mines Company and Oscar W. Worthwine for the month of November, 1950, which would become due December 20, 1950, shall be postponed until December 20, 1951, at which time the said Bradley Mining Co. shall pay the same.

(2) It is further agreed that the said Bradley Mining Co. shall make the usual monthly reports as to moneys received by it during the preceding month upon which royalties would be payable, stating the amounts of royalties that had accrued, but, instead of sending the check as has been the practice during the past ten years, shall make a notation thereon to the effect that "the above accrued royalty has been postponed for a period of one (1) year from the.....day of....., 1950, to the..... day of....., 1951, at which time the same shall become payable".

(3) Save and except for the above and foregoing postponement of royalties, the said Conveyance and Royalty Agreement, in all of its particulars and provisions, shall remain in full force and effect.

Defendant's Exhibit No. 6—(Continued)

In Witness Whereof United Mercury Mines Company, an Idaho corporation has hereunto caused its corporate name to be subscribed, and its corporate seal to be hereunto affixed, duly attested by its Secretary, pursuant to resolution duly adopted by its Board of Directors; Oscar W. Worthwine, one of the parties of the first part, has hereunto set his hand and seal; and Bradley Mining Co., a corporation, the party of the second part, has hereunto caused its corporate name to be subscribed by its Vice-President, and its corporate seal to be hereunto affixed, duly attested by its Secretary, pursuant to resolution duly adopted by its Board of Directors, on this 20th day of July, 1950.

UNITED MERCURY MINES
COMPANY,

By J. J. OBERBILLIG,

[Seal] OSCAR W. WORTHWINE,
Parties of the First Part;

Attest: Veda Steil, Its Ass't Secretary.

[Seal] BRADLEY MINING CO.,
a corporation,

By JOHN D. BRADLEY,
Its Vice-President,
Party of the Second Part.

Attest: E. A. Griffen, Its Secretary. [Seal]

PLAINTIFF'S EXHIBIT No. 11

[Letterhead of Bradley Mining Co.]

Air Mail

April 14, 1948

Mr. John J. Oberbillig, President,
United Mercury Mines Co.,
256 Sonna Building,
Boise, Idaho.

Dear John:

Your letter of April 12 in reply to mine of March 31 arrived yesterday, and as I did not understand your reply to the proposal contained in my letter, I telephoned Oscar Worthwine yesterday afternoon thinking that perhaps he had had a chance to explore the situation with you and learn your reactions.

Oscar advised me that he believes you have in mind that should the smelter be constructed on our property, there should be no deduction for normal smelter charges and that accordingly the 5% royalty should apply on net smelter proceeds. Oscar was not clear on your proposal for aiding us in financing the smelter. If the foregoing interpretation of your thinking is correct, then the following is my reaction:

First, although we appreciate your intentions, we are not asking you to aid us in financing the smelter. Secondly, if you have in mind that if the smelter were located on Yellow Pine Mine property that in such instance normal smelter charges should not be deducted prior to calculating the 5% royalty,

Plaintiff's Exhibit No. 11—(Continued)

then in that case I feel you do not completely understand the situation.

The present 5% royalty rate on net smelter returns was based on the Yellow Pine Mine property with the metallurgical improvements limited to concentrating facilities. Naturally, even after the smelter is built if raw concentrates such as tungsten are shipped, then the 5% royalty rate would apply. The further metallurgical step of reducing the concentrates requires an entirely different basis for royalty computation. I have endeavored to explain this in some detail in my letter of March 31 and I would appreciate your rereading and studying the points outlined.

Oscar Worthwine stated that he did not understand what normal smelter charges were, and asked if I would explain this further. In this connection I am enclosing herewith a memo from the Bunker Hill Smelter outlining how they determine normal smelting charges. Heretofore in discussing the situation with you and writing you about it, I have indicated that normal smelter charges include not only treatment charges but also metal or metallurgical deductions and quotational deductions. In applying this common smelter practice to the case of our shipments, I have suggested that the precedent of several years of our shipments be used as a guide in determining what would be a normal smelter charge, which we then feel would be fair to apply at our new Stibnite smelter. To give an estimated breakdown on costs involved in current shipments

Plaintiff's Exhibit No. 11—(Continued)

I present the following, which, of course, can only be an estimate as we do not know our consumers' costs. Example—The Harshaw Chemical Company:

Assumption 50% Sb concentrates — market price
33c/# f.o.b. Western points

Estimated Harshaw Chemical net sales price converted back to tons of concentrate: \$350/ton (incl. Au & Ag).

Cost of concentrates to H. C. Co., 210* (incl. Au. & Ag).

Harshaw profit and treatment costs: 140.

Estimated Harshaw treatment costs: 75.

Estimated Harshaw profit: \$65/ton.

*Harshaw pay to B. M. Co. at El Segundo: \$210.

Less truck and R.R. frt. to El Segundo: 20.

B. M. Co. net at Stibnite: \$190.

In view of the above, we believe the correct Stibnite smelter treatment charge per ton of raw concentrates should be, under similar conditions of price and grade, \$165/ton (Harshaw sales value \$350, minus B. M. Co. receives at Cascade \$185 = \$165).

Rather than endeavoring to determine the correct smelting charge to be applied against each ton of raw concentrates, we prefer the simplified procedure of applying a royalty rate which will reflect the normal smelter charges and which will at the same time actually increase the returns to the United Mercury Mines Co.

Plaintiff's Exhibit No. 11—(Continued)

In arriving at the suggested 2.75% rate to replace the 5% royalty rate in the instance of locally smelted concentrates, we have applied the following procedure:

$0.05 \times \$190 = \9.50 royalty/ton of concentrate to U. M. M. Co.

$0.0275 \times 350 = 9.65$ royalty/ton of concentrate to U. M. M. Co.

In contrast to arriving at the simplified procedure of applying a flat 2.75% royalty rate for locally reduced concentrates, we could, of course, use as a base our actual operating costs at Stibnite plus other charges that would be made by any competing smelter. A third method of arriving at the normal smelting charges would be periodically to offer our different concentrates to various smelters accepting those types of concentrates in order to arrive at the pay for the metals contained in those concentrates. We could then use such bids offered for our different types of concentrates as a basis for arriving at our smelting costs at Stibnite. Of course, the great disadvantages to these latter alternatives would be that they might leave room for petty disputes.

Although today we are approving preliminary arrangements for the construction of a smelter to reduce our Yellow Pine Mine concentrates, we have not yet decided on the exact location of the reduction plant. We intend to proceed, however, with the roasting facilities at Stibnite and the placing of orders for the electric furnace and the refining and converting equipment. At a later date we will make

Plaintiff's Exhibit No. 11—(Continued)

the final decision as to the location of this reduction plant.

In view of the high cost of building 40 homes at Stibnite (\$250,000 including water, electric and sewerage facilities), we are seriously considering Cascade as the location of our reduction plant. The reduction plant, of course, would take by far the greater majority of the smelter crew; i.e., there would be very few men allocated to the roasting department, so that housing at Stibnite for the roasting plant alone would not be a problem. This may appear like an uneconomical move in view of the transportation of calcines by truck to Cascade. However, there are several compensating factors—one, I have already mentioned a possible substantial saving in housing; two, for an eventual custom smelter business a location on a railhead for the reduction plant would have certain advantages for the Northwest as a whole—although I can see certain disadvantages for other properties in the Yellow Pine Mining District; three, the incoming tonnage for reagents, etc. would greatly aid in offsetting the outgoing tonnage of calcines which would be substantially reduced in weight over the raw concentrates. We are presently exploring the housing situation in Cascade.

Whether or not the complete smelter is constructed at Cascade or Stibnite, the smelter will have to be an entirely separate division from the Yellow Pine Mine and its concentrating plant from an operating, accounting, and taxation standpoint.

Plaintiff's Exhibit No. 11—(Continued)

In other words, it is a separate venture and should not be tied in with the royalty schedule of Yellow Pine Mine as it now stands.

We should make a final decision on the location of the reduction plant by June 1. The attitude you are going to take on this entire subject will naturally affect a decision as to location. Accordingly, I would appreciate your reactions at the earliest date possible; particularly since I will not return to Idaho for at least ten days.

Very truly yours,

/s/ John D. Bradley,

Executive Vice President.

JDB:MM Enc. cc: OWW

DEFENDANT'S EXHIBIT No. 21

[Rejected]

[Letterhead of Oscar W. Worthwine]

December 30, 1941

Bradley Mining Company,
425 Crocker Building,
San Francisco, California.

Attention: John D. Bradley.

Dear Sirs:

John and I have gone over Mr. Davis' letter and have made the corrections suggested by him and I am herewith enclosing an original and two copies of the corrected pages that I have rewritten, the corrections being as follows:

Defendant's Exhibit No. 21—(Continued)

Page 16—About the middle of the page in caps appears the word "SOLD", this should be changed to "HOLD". I have not rewritten this page because the correction can easily be made on the three copies which you have in your possession.

Page 12—I have rewritten page 12 by inserting in the next to the last line after the word 'operations' and the word 'upon' the following "and development work."

This is to comply with the suggestion made by Mr. Davis under subdivision (4) on page 3 of his letter of December 26th.

Page 17—Failure to do assessment work. I have rewritten this page by adding at the end of paragraph I the following:

"failure by Bradley to do said assessment work shall not work a forfeiture of the grant and conveyance hereinbefore made."

This is to comply with the suggestion made by Mr. Davis under subdivision (b) on page one in regard to the doing of assessment work.

Page 22—I have rewritten page 22 but adding at the end of paragraph VII the following:

"and failure to give a written notice of its election not to proceed under this option shall not be considered as an election to proceed under this option."

This is to overcome the objection made by Mr. Davis to subdivision (c) on page 2 of his letter.

I suggest you take the three copies of option I sent you and take out the pages that are now in

Defendant's Exhibit No. 21—(Continued)

and insert the enclosed pages, and your stenographer can make the correction on page 16 where the word 'sold' is to be changed to 'hold.'

I believe these corrections meet all the suggestions made by Mr. Davis except the matter of title concerning which I wrote you on yesterday.

Taxes: While the memorandum brief which I sent you suggests that I have read a few decisions by the Supreme Court of the United States in regard to depletion I did not pretend and do not now claim to have made any exhaustive study of this matter.

On page 4 of his letter Mr. Davis refers to an opinion by J. P. Wenchel of the Bureau of Internal Revenue. I have read that opinion and still I am not certain but that the Internal Revenue Department and the Courts will hold that the particular arrangement here is a sale and that the United will not be entitled to depletion. Mr. Wenchel in his opinion states that the rule adopted by the Supreme Court of the United States is that if a gross royalty is to be paid the Lessor is entitled to take depletion, while if a net royalty is to be paid the Lessor is not entitled to take depletion.

Under the arrangement that the United is now making with Bradley we are not receiving a gross royalty. This is because we are agreeing to allow Bradley \$2.50 per ton for each ton of concentrates shipped. However, on this particular point it is probable that the Supreme Court will hold that it is more nearly a gross royalty than a net royalty.

Defendant's Exhibit No. 21—(Continued)

This because of the almost uniform and universal practice of allowing the deduction of freight, assay, and smelting charges from what we ordinarily consider to be a net royalty. However, in view of the opinion given you by your tax consultants I assume you are satisfied with this tax matter.

If the entire contract is now satisfactory I suggest that your Board of Directors approve it and that we be furnished with certified copy of Resolution approving it, and that it be signed by your officers with the attesting seal of the corporation impressed thereon. Then the United can sign the copies which you bring with you and then we can have the stockholders and directors approve and ratify the acts of the President and Secretary in entering into this contract.

John advises me he does not anticipate the slightest difficulty in having the stockholders and directors approve this transaction.

Yours very truly,

/s/ Oscar W. Worthwine.

OWW:W encls

DEFENDANT'S EXHIBIT No. 22

[Rejected]

[Letterhead of Oscar W. Worthwine.]

December 30, 1941

Bradley Mining Company,
425 Crocker Building,
San Francisco, California.

Attention: John D. Bradley.

Dear John:

Re: Conveyance, Royalty Agreement and Option

On yesterday I sent you certain pages which I had rewritten with the suggestion that you insert the same in the agreement in lieu of the ones originally placed therein.

In the sheets I sent you yesterday I only made one change on page 12 which was the addition of the words "and development work" in the second line from the bottom.

I am enclosing three copies of page 12 which I have again rewritten, and I am also enclosing one copy of page 12 to which is attached a note to the effect that it is not to be inserted in the agreement. The reason I am enclosing this sheet is because I have underscored for your reference the changes which I believe should be made in respect to the \$2.50 per ton allowance for trucking.

In drawing the instrument about two weeks ago I made no change whatsoever in the provisions of the 1939 contract in regard to the \$2.50 allowance per ton for trucking, but if you will examine page

Defendant's Exhibit No. 22—(Continued)

12 carefully or the provisions of the 1939 contract in regard to the \$2.50 per ton allowance you will note it contemplates only the shipment of concentrates or products to a smelter. In other words, there may be room for the contention that when you ship concentrates to the General Electric that you are not shipping to a smelter, and therefore you would not be entitled to the \$2.50 allowance. Then in time you may produce something other than concentrates which would be shipped to other than a smelter. If you found a cinnabar deposit you would not ordinarily ship your product to a smelter, and I believe we should include the words: "to market" and "market returns".

So much for straightening out the paragraph so that it will prevent any claim being presented against your company.

On the other hand, looking at it from the standpoint of the United, it might be that in the future a mill or smelter will be erected at Yellow Pine and certainly it was not the intention of the parties that you would be allowed \$2.50 per ton haul for ore from Stibnite to Yellow Pine. Consequently, as I have redrafted this paragraph and as shown by the enclosed copy which contains the underscoring I have limited the allowance of \$2.50 per ton to concentrates or products to the Couer d'Alenes or to a market or smelter outside the state of Idaho.

I believe it was the intention of the parties when the 1939 contract was drawn that you should be permitted \$2.50 per ton for all shipments made

Defendant's Exhibit No. 22—(Continued)

from Cascade by rail or all truck shipments made from Stibnite to Kellogg as well as any shipment by truck from Stibnite to Salt Lake or other points. I likewise believe it was the intention of the parties that you should have the \$2.50 per ton allowance whether you shipped to a smelter or sold your products to a consumer.

Therefore, if a new contract is entered into this paragraph should be so worded that no board of directors of the United could ever contend you were not entitled to the \$2.50 allowance for shipments made to Kellogg or points outside the state of Idaho even though such shipments did not go to a smelter.

I am not worried about you or your family contending that you could put a mill or smelter at Yellow Pine or some other point off this particular property and be entitled to \$2.50 per ton for transporting the ores from the property to the mill or smelter, but if control of this property should pass from you and your family I do not desire it to be possible for your successors to contend that by building a mill at Yellow Pine or some other place nearby that they would be entitled to a haulage charge of \$2.50 per ton for ores.

As I wrote you yesterday in my opinion the question of whether this is a sale so that the respective parties will not be entitled to depletion, or whether it is a transaction under which each party will be entitled to depletion depends on whether the United is entitled to a royalty on the gross or a royalty on the net, and in my opinion the changes I have sug-

Defendant's Exhibit No. 22—(Continued)
gested above bear on this point because it is conceivable that if you were allowed \$2.50 per ton from a point as near by as Yellow Pine there would never be any net for United.

Therefore I suggest that it is to the advantage of both parties that the enclosed unmarked copies of page 12 be inserted in the agreement in lieu of the one mailed you yesterday.

Wishing you a happy and successful New Year,
I am

Yours very truly,

/s/ Oscar W. Worthwine.

OWW:W encl

PLAINTIFF'S EXHIBIT No. 26

[Title of District Court and Cause.]

PLAINTIFF'S REQUEST FOR ADMISSIONS

Plaintiff, United Mercury Mines Company, requests Defendant, Bradley Mining Co., within fifteen (15) days after service of this request, to make the following admissions for the purpose of this action only, and subject to all pertinent objections to admissibility which may be interposed at the trial:

1. That each of the following documents exhibited with this request, copies of which are attached, is genuine.

(a) Copy of letter dated January 29, 1942 to Mr. George K. Dorsey, Reynolds & Co., 1500 Walnut

Plaintiff's Exhibit No. 26—(Continued)
Street, Philadelphia, Pa., from John D. Bradley,
signed with initials "J.D.B."

(b) Letter dated March 17, 1947, addressed to
Mr. John J. Oberbillig, President, United Mercury
Mines Company, 256 Sonna Building, Boise, Idaho,
relative to Antimony Ridge Group, including
Golden Gate Claims, from Bradley Mining Co.,
signed by John D. Bradley as Vice President.

/s/ PAUL S. BOYD,
/s/ E. H. CASTERLIN,
/s/ DALE CLEMONS,
Attorneys for Plaintiff.

Acknowledgment of Service attached.

(Copy)

For: J. J. Oberbillig, 258 Sonna Bldg., Boise,
Idaho.

Mr. George K. Dorsey, January 29, 1942
Reynolds & Co.,
1500 Walnut Street, Philadelphia, Pa.

Dear Sir:

Your letter of the 17th inst. addressed to my
father, the late F. W. Bradley, has been received.

The Yellow Pine Company has been superseded
by the Bradley Mining Co. as the operator of the
Yellow Pine Mine previously owned by the United
Mercury Mines Co.

On January 1st, 1942, a new agreement between
United Mercury Mines Co. and Bradley Mining Co.
was concluded whereby title to the property passed

Plaintiff's Exhibit No. 26—(Continued)
to the Bradley Mining Co. and the latter company
thereby agrees to pay the United Mercury Mines
Co. a perpetual 5% royalty on the net sales pro-
ceeds.

On the 1941 production the royalties payable to
United Mercury Mines Co. amount to \$66,000.

For further information please contact Mr. J. J.
Oberbillig, 258 Sonna Building, Boise, Idaho.

Yours very truly,

/s/ J.D.B.

JDB:CFd—cc. J. J. Oberbillig.

Bradley Mining Co.

P.O. Box 737, Boise, Idaho

March 17, 1947

Mr. John J. Oberbillig, President

(Copy)

United Mercury Mines Company

256 Sonna Building, Boise, Idaho

Re: Antimony Ridge Group, including Golden
Gate Claims

Dear John:

Confirming our several telephone conversations of
this morning, this is to advise you of our wish that
you proceed with Mr. Worthwine in the prepara-
tion of a conveyance and royalty agreement for the
Antimony Ridge Group and the Golden Gate claims
similar to our recent conveyance for the Midnight
Group, for the consideration of \$7,500.00 to be paid
at the time of consummating the agreement.

As you know under the arrangement for the Mid-
night Group, it was taken over by the Bradley

Plaintiff's Exhibit No. 26—(Continued)

Mining Co. under the same terms and conditions under which we took over the Meadow Creek and Hennessey Groups at Stibnite. Under this arrangement we are to pay a 5% perpetual gross royalty.

It occurs to me that the advantage to you and your stockholders is that the United Mercury Mines Company will receive a 5% gross royalty from any ores mined, shipped and sold from any property, whether from the Meadow Creek, Hennessey, Mid-night or Antimony Ridge groups. This will simplify the keeping of records as it will not be necessary for us to keep a separate record of ores taken from any one group. We also believe that if there is common ownership of the entire group we will have somewhat more freedom in applying work and labor done in one place on the claims in all the groups.

Bradley Mining Co. will also either give you a letter or a separate agreement to the effect that if it desires to abandon any of the claims in the Antimony Ridge Group that it will, on or before April 1 in any year, give you a quitclaim deed to the same so that you will have sufficient time to begin the assessment work on such surrendered claims during the assessment year.

With kind regards, I am

Sincerely yours,

Bradley Mining Co.

/s/ John D. Bradley,

Executive Vice President

JDB:mk

[Endorsed]: Filed October 15, 1954.

PLAINTIFF'S EXHIBIT No. 26-A

[Title of District Court and Cause.]

RESPONSE TO REQUEST FOR ADMISSIONS

State of California,

City and County of San Francisco—ss.

John D. Bradley, being first duly sworn on oath deposes and says: That he is Executive Vice-President of Bradley Mining Co., a corporation, the defendant above named, and makes the following admissions and denials in response to the Request for Admissions served on the defendant by the plaintiff on October 15, 1954.

Request No. 1(a): Defendant admits that the letter referred to in Request No. 1(a) is genuine, but alleges that said letter and the contents thereof are irrelevant, improper and immaterial to the issues in this case, for the reason that the matters and things contained in said letter have no proper relation to and are not material to the question of defendant's alleged liability for the payment of additional royalties under the Conveyance and Royalty Agreement of December 31, 1941.

Request No. 1(b): Defendant admits that the letter referred to in Request No. 1(b) is genuine, but alleges that said letter and the contents thereof are irrelevant, improper and immaterial to the issues in this case, for the reason that the matters and things contained in said letter have no proper relation to and are not material to the question of defendant's alleged liability for the payment of

Plaintiff's Exhibit No. 26-A—(Continued)
additional royalties under the Conveyance and
Royalty Agreement of December 31, 1941.

Dated this 29th day of October, 1954.

/s/ JOHN D. BRADLEY,
Executive Vice-President
Bradley Mining Co.

Subscribed and sworn to before me this 29th day
of October, 1954.

[Seal] /s/ AGNES WESTRA,
Notary Public in and for the City and County of
San Francisco, State of California.

Acknowledgment of Service attached.

[Endorsed]: Filed November 2, 1954.

PLAINTIFF'S EXHIBIT No. 27

[Title of District Court and Cause.]

INTERROGATORIES BY PLAINTIFF

To Bradley Mining Company, Defendant,—

The plaintiff requests that the following inter-
rogatories be answered under oath by any of your
officers competent to testify in your behalf who
knows the facts about which inquiry is made and
that the answers be served on plaintiff within 15
days from the time the same were served on you.

Interrogatory No. 1. What is the (a) amount,

Plaintiff's Exhibit No. 27—(Continued)

(b) character and (c) mineral content of all minerals, ores, metals or values mined, extracted or taken from the mining claims described in "Exhibit I" attached to plaintiff's complaint, immediately before the same were smelted, processed or treated at the Yellow Pine Smelter, so-called, during the period from July 1949 to date?

Interrogatory No. 2. What is the (a) amount, (b) character and (c) mineral content of the smelted product from said minerals, ores, metals or values mentioned in Interrogatory No. 1?

Interrogatory No. 3. Have any of the smelted products mentioned in Interrogatory No. 2 been sold by you to third parties?

Interrogatory No. 4. If your answer to Interrogatory No. 3 is in the affirmative, then give the name or names of the purchasers of the same.

Interrogatory No. 5. If your answer to Interrogatory No. 3 is in the affirmative, then give the (a) name of the saleable product so sold, (b) the amount of the same so sold, and (c) the amount of money received from the sale thereof before any deductions for marketing and shipping costs from Cascade, Idaho.

Interrogatory No. 6. If your answer to Interrogatory No. 3 is in the affirmative, then state the marketing and shipping costs connected with each sale or sales named in answer to Interrogatory No. 5.

Plaintiff's Exhibit No. 27—(Continued)

Dated November 2d, 1953.

/s/ PAUL S. BOYD,

/s/ E. H. CASTERLIN,

/s/ DALE CLEMONS,

Attorneys for Plaintiff.

Acknowledgment of Service attached.

[Endorsed]: Filed November 2, 1953.

PLAINTIFF'S EXHIBIT No. 27-A

[Title of District Court and Cause.]

DEFENDANT'S ANSWERS TO PLAINTIFF'S
INTERROGATORIES

State of Idaho,
County of Ada—ss.

John D. Bradley, Being first duly sworn on oath
deposes and says:

That he is Executive Vice-President of Bradley Mining Co., a corporation, the defendant above named, and hereby answers, in accordance with Rule 33 of the Federal Rules of Civil Procedure, the Interrogatories served upon the defendant by the plaintiff (except those interrogatories to which objections have been filed) as follows:

Interrogatory No. 1. What is the (a) amount, (b) character and (c) mineral content of all minerals, ores, metals or values mined, extracted or taken from the mining claims described in "Ex-

Plaintiff's Exhibit No. 27-A—(Continued)
hibit I" attached to plaintiff's complaint, immediately before the same were smelted, processed or treated at the Yellow Pine Smelter, so-called, during the period from July 1949 to date?

(a) The amount of all minerals, ores, metals or values mined, extracted or taken from the mining claims described in "Exhibit I" attached to plaintiff's complaint, immediately before the same were smelted, processed or treated at the Yellow Pine Smelter of the defendant during the period July 1949 to November 2, 1953, was 28,449.835 tons of concentrates.

(b) The character of all such minerals, ores, metals or values immediately before the same were smelted, processed or treated at the Yellow Pine Smelter during the period from July 1949 to November 2, 1953, consisted of antimony concentrates and gold concentrates.

(c) The mineral content of such concentrates, as evidenced by royalty statements heretofore furnished the plaintiff, is set forth on schedule marked "Exhibit A" hereto attached and hereby made a part hereof, which schedule shows the percentage of each metal contained in each lot of concentrates therein listed and the total amount thereof in pounds or ounces.

Interrogatory No. 2 Objection filed.

Interrogatory No. 3 Objection filed.

Interrogatory No. 4 Objection filed.

Plaintiff's Exhibit No. 27-A—(Continued)

Interrogatory No. 5 Objection filed.

Interrogatory No. 6 Objection filed.

/s/ JOHN D. BRADLEY,

Executive Vice-President of
Bradley Mining Co.

Subscribed and sworn to me before this 10th day
of November, 1953.

[Seal] /s/ RALPH R. BRESHEARS,
Notary Public for the State of Idaho residing at
Boise, Idaho.

EXHIBIT "A"

SCHEDULE

	Character		
	Gold	Antimony	Total
	Concentrate	Concentrate	Concentrate
Dry Tons	8,398.465	20,051.370	28,449.835
Calculated Average Assays:			
Gold—ounces per ton	2.232	0.721	
Silver—ounces per ton	4.766	12.891	
Antimony—%	5.828	37.398	
Contents:			
Gold—ounces	18,750.305	14,458.119	33,208.424
Silver—ounces	40,026.37	258,477.08	298,503.45
Antimony—pounds	979,025.	14,997,505.	15,976,530.

Acknowledgment of Service attached.

[Endorsed]: Filed November 10, 1953.

PLAINTIFF'S EXHIBIT No. 27-B

[Title of District Court and Cause.]

DEFENDANT'S ANSWERS TO PLAINTIFF'S
INTERROGATORIES

State of Idaho,
County of Shoshone—ss.

John D. Bradley, being first duly sworn, on oath deposes and says:

That he is Executive Vice President of Bradley Mining Co., a corporation, the defendant above named, and hereby answers in accordance with Rule 33 of the Federal Rules of Civil Procedure—and pursuant to the memorandum decision of acting District Judge Healy filed in the above entitled court on April 9, 1954, the Interrogatories served upon the defendant by the plaintiff, as follows:

Interrogatory No. 1. What is the (a) amount, (b) character, and (c) mineral content of all minerals, ores, metals or values mined, extracted or taken from the mining claims described in "Exhibit I" attached to plaintiff's complaint, immediately before the same were smelted, processed or treated at the Yellow Pine Smelter, so-called, during the period from July 1949 to date?

Plaintiff's Exhibit No. 27-B—(Continued)

Answer:

(a)	(b)	(c)		
		Metal Content		Antimony
Amount— Dry Tons	Character	Gold-Oz.	Silver-Oz.	Lbs.
8,398.465	Gold Concentrate	18,750.305	40,026.37	979,025
20,051.370	Antimony Con- centrate	14,458.119	258,477.08	14,997,505
28,449.835	Total	33,208.424	298,503.45	15,976,530

All as shown in Exhibit A attached (previously supplied).

Interrogatory No. 2. What is the (a) amount, (b) character, and (c) mineral content of the smelted product from said minerals, ores, metals or values mentioned in Interrogatory No. 1?

Answer:

The amount, character and mineral content of the smelted product for which information is requested is set forth below and in "Exhibit B" attached hereto.

(a)	(b)	(c)		
		Metal Content		Antimony
Amount— Lbs.	Character	Gold-Oz.	Silver-Oz.	Lbs.
12,727,033	Oxide			10,563,438
211,412	Metal			210,306
179	High Purity Metal			179
360,524	Residue	26,915.682	249,062.44	225,992
97,989	Calcine	160.947	286.13	1,666
Total Finished Products		27,076.629	249,348.57	11,001,581
Remaining in process				
Secondary unfinished prod- ucts and absorption		1,693.671	15,360.07	1,144,402
Total Finished and Unfinished Products		28,770.300	264,708.64	12,145,983

Plaintiff's Exhibit No. 27-B—(Continued)

Interrogatory No. 3. Have any of the smelted products mentioned in Interrogatory No. 2 been sold by you to third parties?

Answer: Yes.

Interrogatory No. 4. If your answer to Interrogatory No. 3 is in the affirmative, then give the name or names of the purchasers of the same.

Answer: The names of the purchasers of the smelted products referred to in Interrogatory No. 3 are shown in the information set forth in the schedules attached to "Exhibit C" filed herewith.

Interrogatory No. 5. If your answer to Interrogatory No. 3 is in the affirmative, then give the (a) name of the saleable products so sold, (b) the amount of the same so sold, and (c) the amount of money received from the sale thereof before any deductions for marketing and shipping costs from Cascade, Idaho.

Answer: The information requested in this interrogatory is set forth below, with further detail in "Exhibit C" herewith, and the schedules attached thereto.

(a)	(b)	(c)
Name	Amount - Lbs.	Amount Money Received before any deductions
Oxide	10,463,433	\$3,598,610.60
Metal	160,812	59,779.76
H. P. Metal	179	388.25
Residue	360,524	1,140,775.48
Calcine	97,989	4,248.66
	Total	<hr/> \$4,803,802.75

Plaintiff's Exhibit No. 27-B—(Continued)

Interrogatory No. 6. If your answer to Interrogatory No. 3 is in the affirmative, then state the marketing and shipping costs connected with each sale or sales named in answer to Interrogatory No. 5.

Answer: The information requested concerning the marketing and shipping costs connected with sales referred to in Interrogatory No. 5 is set forth below and in "Exhibit C" herewith and the schedules attached thereto.

Freight paid	\$84,256.11	
Miscellaneous Allowances	31.91	\$84,288.02

/s/ JOHN D. BRADLEY,
Executive Vice President of
Bradley Mining Co.

Subscribed and sworn to before me this 12th day of May, 1954.

[Seal] /s/ HARRIET I. BERGMAN,
Notary Public, in and for the County of Shoshone,
State of Idaho.

Acknowledgment of Service attached.

[Printer's Note: Exhibit "A" attached hereto is a duplicate of Exhibit "A" set out in full at page 403 of this printed record.]

[Endorsed]: Filed May 17, 1954.

PLAINTIFF'S EXHIBIT No. 28

[Title of District Court and Cause.]

REQUEST FOR ADMISSIONS

Plaintiff United Mercury Mines Company, a corporation, requests the defendant Bradley Mining Company, a corporation, within fifteen days after the service of this request to make the following admissions for the purpose of this action only and subject to all pertinent objections to admissibility which may be interposed at the trial:

1.

That the following document, a copy of which is marked "Exhibit 1" and attached to plaintiff's complaint filed herein, is genuine,—

Conveyance, Royalty Agreement and Option dated December 31st, 1941, between this plaintiff, called "United" and this defendant, called "Bradley"

2.

That each of the following statements is true:—

(a) That the plaintiff is a citizen of the State of Idaho; that the defendant is a citizen of the State of California; that the amount in controversy exceeds, exclusive of interest and costs, the sum of Three Thousand Dollars.

(b) That on or about December 31st, 1941, United Mercury Mines Company and Bradley Mining Company entered into an agreement in writing dated that day, a true copy of which is marked "Ex-

Plaintiff's Exhibit No. 28—(Continued)

hibit 1" and is attached to plaintiff's complaint filed herein.

(c) That pursuant to the terms of said agreement, United Mercury Mines Company has conveyed to the Bradley Mining Company all of the mining claims and other property described in said agreement.

(d) That during the year 1949 Bradley Mining Company completed the construction of a smelter, commonly known as the Yellow Pine Smelter, on the mining ground described in the said agreement, at its own costs and expense.

(e) That Bradley Mining Company is now and at all times mentioned in the complaint filed herein has been the sole owner of said Yellow Pine Smelter.

(f) That Bradley Mining Company first put the said Yellow Pine Smelter into operation during the month of July, 1949.

(g) That from and after December 31st, 1941, Bradley Mining Company has mined, extracted and taken from the mining claims described in the said agreement minerals, ores, metals and values of various kinds among which are gold, silver, antimony, tungsten, sulphur, arsenic and copper.

(h) That from December 31, 1941 to July 1949, Bradley Mining Company transported or caused to be transported, pursuant to the terms of said agreement, all of the said minerals, ores, metals

Plaintiff's Exhibit No. 28—(Continued)

and values that were treated, smelted or processed under the terms of said agreement to smelters or reduction plants located at a distance from the said mining claims, in which neither United Mercury Mines Company nor Bradley Mining Company had any interest of any kind whatever and which were foreign to the said agreement.

(i) That from and after July 1st, 1949, Bradley Mining Company transported or caused to be transported, pursuant to the terms of said agreement, only a small portion of said minerals, ores, metals and values that were extracted from said mining claims and that were treated, smelted or processed under the terms of said agreement to smelters or reduction plants located at a distance from the said mining claims and which were absolutely foreign in all respects to said agreement and the respective parties to this action.

(j) That upon receipt of the net smelter returns as defined in said agreement from the said foreign smelters or reduction plants, being those located at a distance from the said mining claims in which neither party to this action had any interest, Bradley Mining Company rendered to United Mercury Mines Company appropriate statements, in each instance after the form rendered to the plaintiff for the month of December, 1948, a true copy of which is marked "Exhibit 2" and attached to the complaint filed herein.

(k) That Bradley Mining Company, upon receipt

Plaintiff's Exhibit No. 28—(Continued)

of the said net smelter returns from the said foreign smelters or reduction plants as defined herein, paid United Mercury Mines Company a royalty of five per cent of said receipts as provided in said agreement, at the time and in the manner prescribed in said agreement.

(l) That from and after the receipt of the net smelter returns as defined in the said agreement, from the said smelters or reduction plants located distant from the said mining claims and in which neither party to this action had any interest whatever, Bradley Mining Company had no right, title, interest, claim and/or demand in and to said minerals, ores, metals and values mined, extracted or taken from the said mining claims, or any part thereof, and the same were the property of the said smelters.

(m) That from and after July 1st, 1949, Bradley Mining Company processed through the Yellow Pine Smelter the greater part of the minerals, ores, metals and values extracted from the said mining claims, being all that were not processed by a foreign smelter.

(n) That after Bradley Mining Company has so processed the said minerals, ores, metals and values extracted from the said mining claims in the Yellow Pine Smelter, the saleable products resulting therefrom are held and retained by the Bradley Mining Company as its sole property until the same are sold to a purchaser.

Plaintiff's Exhibit No. 28—(Continued)

(o) That Bradley Mining Company has sold to purchasers saleable products resulting from the smelting and reduction of minerals, ores, metals and values taken from the said mining claims in the Yellow Pine Smelter.

(p) That the Bradley Mining Company has sold to purchasers saleable products resulting from the smelting and reduction of minerals, ores, metals and values extracted, mined and taken from the mining claims described in said agreement, in the Yellow Pine Smelter.

(q) That the Bradley Mining Company has not paid to United Mercury Mines Company as royalty a sum or sums of money equal to five per cent of the amount or amounts paid by any purchaser or purchasers from the sale of saleable products obtained from the concentrates, ores, metals or values shipped, taken or produced from the mining claims described in said agreement, less marketing and shipping costs as defined in said agreement.

Dated September 14, 1953.

PAUL S. BOYD, E. H. CASTERLIN
and DALE CLEMONS,
Attorneys for Plaintiff herein.

/s/ By PAUL S. BOYD.

Acknowledgment of Service attached.

[Endorsed]: Filed September 17, 1953.

PLAINTIFF'S EXHIBIT No. 28-A

[Title of District Court and Cause.]

RESPONSE TO REQUEST FOR ADMISSIONS

State of California,
City and County of San Francisco—ss.

John D. Bradley, being first duly sworn, on oath deposes and says:

That he is Executive Vice President of Bradley Mining Co., a corporation, the defendant above named, and makes the following admissions and denials on the Request for Admissions served on the defendant on the 17th day of September, 1953, by the plaintiff.

Request No. 1. Defendant admits the matters stated therein.

Request No. 2 (a). Defendant admits the matters stated therein.

Request No. 2 (b). Defendant admits the matters stated therein.

Request No. 2 (c). Defendant admits the matters stated therein.

Request No. 2 (d). Defendant admits the matters stated therein.

Request No. 2 (e). Defendant admits the matters stated therein.

Request No. 2 (f). Defendant admits the matters stated therein.

Request No. 2 (g). Defendant denies each and

Plaintiff's Exhibit No. 28-A—(Continued)
every matter and thing stated therein, and in this connection defendant admits that from and after December 31, 1941, defendant has mined, extracted and taken from the mining claims described in the agreement between the parties dated December 31, 1941, ores containing—and principally valuable for—gold, silver, antimony, and tungsten; that no copper was recovered from such ores; that such ores contained sulphur for which no payments were received, and that such ores also contained arsenic for which smelter penalties were charged.

Request No. 2 (h). Defendant denies each and every matter and thing stated therein, and in this connection defendant admits that from December 31, 1941, to July, 1949, defendant shipped—pursuant to the terms of said agreement—concentrates produced from ores mined and extracted from said claims to smelters or reduction plants located at a distance from said mining claims, which smelters or reduction plants were not owned or controlled by defendant and which were not parties to said agreement of December 31, 1941—such smelters or reduction plants being hereinafter referred to as “outside smelters.”

Request No. 2 (i). Defendant denies each and every matter and thing stated therein, and in this connection admits the fact to be that after July 31, 1949, it shipped a substantial portion of concentrates which were principally valuable for their gold content to outside smelters; that during said period defendant shipped to outside smelters—based

Plaintiff's Exhibit No. 28-A—(Continued)

on values—approximately forty-five per cent (45%) of concentrates produced from ore mined or extracted from said mining claims.

Request No. 2 (j). Defendant denies each and every matter and thing stated therein, and in this connection admits that as to all concentrates shipped by it to outside smelters, the defendant computed and paid royalties to plaintiff strictly in accordance with the terms of its agreement with plaintiff, and that "Exhibit 2" attached to plaintiff's complaint is a true copy of a report rendered to plaintiff by defendant for the month of December, 1948.

Request No. 2 (k). Defendant denies each and every matter and thing stated therein, and in this connection admits that payment of royalties made by it to plaintiff on account of concentrates shipped to outside smelters was in the amount of five per cent (5%) of net smelter returns received, and that the payments so made were strictly in accord with the agreement between plaintiff and defendant.

Request No. 2 (l). Defendant denies each and every matter and thing stated therein, and in this connection defendant admits that from and after receipt by defendant of the net smelter returns from concentrates shipped to outside smelters, defendant had no right, title or interest in or to such concentrates, the same being the property of said outside smelters.

Request No. 2 (m). Defendant denies each and every matter and thing stated therein, and in this connection defendant admits that from and after

Plaintiff's Exhibit No. 28-A—(Continued)
the completion of the Yellow Pine Smelter in the month of July, 1949, defendant processed through said smelter approximately fifty-five per cent (55%)—based on values—of the concentrates produced from ore mined or extracted from said mining claims.

Request No. 2 (n). Defendant admits the matters stated therein.

Request No. 2 (o). Defendant admits the matters stated therein.

Request No. 2 (p). Defendant admits the matters stated therein.

Request No. 2 (q). Answering this Request, defendant alleges the matters and things set forth in Request No. 2 (q) are irrelevant, improper and immaterial to the issues in this case for the reasons that they have no proper relation to and are not material to the question of defendant's alleged liability for the payment of additional royalties under the conveyance and royalty agreement of December 31, 1941; defendant further admits that it has not paid, and has never been under any obligation to pay United Mercury Mines Company and sum or sums equal to five per cent (5%) of the amount paid to defendant by purchasers of products resulting from defendant's Yellow Pine Smelter operations.

Dated this 28th day of September, 1953.

/s/ JOHN D. BRADLEY,

Executive Vice President of Bradley Mining Co.

Plaintiff's Exhibit No. 28-A—(Continued)

Subscribed and sworn to before me this 28th day
of September, 1953.

[Seal] /s/ AGNES WESTRA,

Notary Public, in and for the City and County of
San Francisco, State of California.

Acknowledgment of Service attached.

[Endorsed]: Filed October 2, 1953.

DEFENDANT'S EXHIBIT No. 29

July 14, 1945

Boise Purification Plant

Lot B-13-B

Sylvania Electric Products Co.

Gross Sales Value per attached

Invoice\$ 34,228.93

Less Operating Costs applicable

including Depreciation 6,295.25

Subject to Royalty.....\$ 27,933.68

Wet Weights for Hauling Allowance

Boise Lot B-13 consisting of:

Lot 223-3

See B-15

222-3

20,430

222-4

19,792

223-1

25,778

66,000

Defendant's Exhibit No. 29—(Continued)

Virgin Quicksilver
Bradley Mining Co.
425 Crocker Building
San Francisco 4, California

Invoice No. B-13B. Lot No. B-13B.

Final Invoice

Sold to Sylvania Electric Products, Inc. Towanda, Pennsylvania.

Shipped to same.

Date May 23, 1945.

Customer's order No. T-9275.

Car. No. Pa 571913.

Routing U.P.,C. & N.W., N. Plate, L.V.

Freight prepaid.

Price \$23.50 per short ton unit.

F.O.B. Towanda, Pa.

Terms: Cash.

Date of shipment from Boise, Idaho, 4/26/45.

427 Sacks Scheelite Concentrate.

Sampled and weighed at Boise, Idaho, by Utah Ore Sampling Co.

Assayed by Gulick-Henderson.

Weights: Total Weight 43,163 lbs. Assays: WO_3 68.03%.

Weights: Tare (Sacks) 256 lbs. Assays: H_2O 0.2%.

Weights: Net Wet Weight 42,907 lbs. Assays: P 0.094%.

Weights: Moisture 86 lbs. Assays: As 0.11%.

Weights: Net Dry Weight 42,821 lbs. Assays: Sb 0.17%.

Defendant's Exhibit No. 29—(Continued)

Weights: WO_3 68.03%. Assays: S 0.36%.

Weights: Content WO_3 29,131.1 lbs. or 1,456.55 S.T.U.

Weights: 1,456.55 S.T.U. @ \$23.50. Assays: \$34,-
228.93.

Papers attached herewith:

Utah Ore Sampling Co. Weight & Moisture Certificate
Gulick-Henderson Co. Assay Certificate.

JPB—GCO

JDB—Boise Office

REB—UMM Co.

HDB

DEFENDANT'S EXHIBIT No. 30

[Title of District Court and Cause.]

PRE-TRIAL CONFERENCE ORDER

Following pre-trial proceedings pursuant to Rule 16 of the Federal Rules of Civil Procedure, It Is Ordered:

I.

United Mercury Mines Company, hereinafter called "United", brought this action against Bradley Mining Company, hereinafter called "Bradley", to obtain a decree interpreting a "Conveyance, Royalty Agreement and Option" contract dated December 31, 1941, between United as the first party thereto and Bradley as the second party thereto, a copy of which said contract is attached to plaintiff's complaint as Exhibit "1". United, by its complaint, prays for judgment against Bradley as follows:

Defendant's Exhibit No. 30—(Continued)

A. That the Court interpret the provisions of said contract and enter its decree herein declaring and decreeing that the proper and legal method for determining the amount of royalty due United from Bradley under the terms of the "Conveyance, Royalty Agreement and Option" for minerals, ores, metals and values extracted or produced from the mining claims described in the agreement and conveyed to Bradley and smelted at the Yellow Pine Smelter owned by Bradley, is by the use of the "net revenue" provision as defined in the agreement;

B. Declaring that it is the duty of Bradley under the terms of said agreement to furnish United the amounts paid by purchasers from the sale of minerals, ores, metals and values extracted from said mining claims and smelted at the Yellow Pine Smelter, and the marketing costs and shipping costs from Cascade, Idaho;

C. That the Court require an accounting by Bradley to United and upon such accounting being had that United have judgment against Bradley for any amount found due, owing and unpaid, and that such amount be declared, as provided in said contract, a mortgage lien in, to and upon the properties therein described;

D. That United have such other and further relief as the Court may deem equitable in the premises, and its costs of suit;

E. The issues are raised by the said complaint and Bradley's answer thereto;

Defendant's Exhibit No. 30—(Continued)

F. Parties: United Mercury Mines Company, plaintiff, and Bradley Mining Company, defendant.

G. The pleadings which raise the issues are

(1) Original Complaint for plaintiff, United Mercury Mines Company, filed July 12, 1951, and

(2) Original Answer of defendant, Bradley Mining Company, filed September 14, 1951.

II.

Federal jurisdiction is invoked upon the grounds:

A. Diversity of citizenship, in that the plaintiff is a citizen of the State of Idaho and the defendant is a citizen of the state of California, licensed to do business in Idaho.

B. That the amount in controversy exceeds the sum of \$3000.00 exclusive of interest and costs.

III.

The admitted facts are as follows:

A. The corporate identity of each of the parties, and the qualification of defendant, Bradley Mining Company, as a California corporation to do business in the state of Idaho. The Court has jurisdiction of the subject matter of and the parties to this action. (Answer and Admissions)

B. The execution of the contract (Exhibit 1, plaintiff's complaint as amended by interlineation) of December 31, 1941, by plaintiff and defendant, and the conveyance by plaintiff, United Mercury Mines Company, to defendant of the property agreed to be conveyed under the said contract, and that defendant became and now is owner of the

Defendant's Exhibit No. 30—(Continued)
Meadow Creek and Henessy Groups of placer and lode mining claims, described in said agreement, subject to the terms and conditions of said agreement, together with all minerals, ores, metals and values contained therein. (Answer and Admissions)

C. That pursuant to said contract defendant mined, extracted and took from the mining properties, minerals, ores, metals and values consisting, among other things, of gold, silver, antimony and tungsten, and prior to commencement of operations of "The Yellow Pine Smelter" the marketable minerals, ores, metals and values were trucked to Cascade, Idaho, and there placed on railroad cars for shipment to smelters or reduction plants located in various parts of the United States and not owned by either plaintiff or defendant, or in which either party had an interest; that monthly statements were rendered by defendant to plaintiff with copies of smelter settlement sheets showing amounts received by defendant and that defendant paid plaintiff five (5%) per cent of the amounts received on the sale of such minerals, ores, metals and values, and that Exhibit 2 attached to plaintiff's Complaint is a true copy of the statement rendered by defendant to plaintiff for the month of December, 1948. (Answer)

That the same practice continued after July 1949 with respect to all shipments to smelters in which neither Bradley nor United had any interest.

D. That in 1949 defendant completed the construction on the mining premises of "The Yellow

Defendant's Exhibit No. 30—(Continued)

Pine Smelter" solely owned by defendant; that defendant operated said smelter and at the time of the action was operating said smelter; that fifty-five (55%) per cent of the concentrates produced from the ores mined from the property were treated in The Yellow Pine Smelter and after completion of the smelting process certain of the products were sold by defendant to purchasers; that as to concentrates treated in the Yellow Pine Smelter defendant has not computed and paid royalties as demanded by plaintiff, in that as to concentrates treated at the Yellow Pine Smelter on the premises, Bradley has not computed and paid royalties based upon sums received from metal sales. (Answer)

E. That Exhibit 3 attached to plaintiff's complaint is typical of the information furnished by defendant to plaintiff with respect to mined material passing through The Yellow Pine Smelter. (Answer)

That Bradley has paid United royalty upon minerals, ores, metals and values passing into the Yellow Pine Smelter based upon net smelter returns in the manner typified by Exhibit 3, attached to the complaint.

F. That an actual controversy exists between the plaintiff and defendant with respect to their rights and other legal relations under said agreement as follows:

1. The provisions of said agreement applicable to the computation and payment of royalties in re-

Defendant's Exhibit No. 30—(Continued)
spect to minerals, ores, metals and values smelted at said Yellow Pine smelter.

2. The nature and extent of the obligation of defendant to furnish to plaintiff information that plaintiff may require to assure it that it is receiving the royalty to which it is entitled.

G. That the action is between citizens of different states and the amount in controversy exceeds the sum of \$3000.00, exclusive of interest and costs. (Answer and Admissions)

H. That Bradley completed construction of the Yellow Pine smelter at its own costs and charges upon the mining claims during the year 1949 and went into operation during July, 1949, and it has at all times been its sole property.

I. That the saleable products resulting from concentrates processed at The Yellow Pine Smelter are held and retained by the Bradley Mining Company as its sole property until the same are sold to a purchaser. (Admissions)

J. That Bradley Mining Company has sold to purchasers saleable products resulting from the smelting and reduction of minerals, ores, concentrates, metals and values taken from the said mining claims and smelted in the Yellow Pine Smelter. (Admissions)

K. That from and after receipt by defendant of the net smelter returns from concentrates shipped to outside smelters defendant had no right, title or interest in or to such concentrates, the same being the property of said outside smelters. (Admissions)

Defendant's Exhibit No. 30—(Continued)

L. That the defendant has sold to purchasers saleable products resulting from the smelting and reduction of minerals, ores, metals and values taken from the said mining claims and smelted in The Yellow Pine Smelter. (Admissions)

M. That defendant has not paid plaintiff sums equal to five (5%) per cent of the amount paid to defendant by purchasers of products resulting from defendant's Yellow Pine Smelter operations. (Admissions)

N. That the books and records of defendant correctly show the amount received by defendant as net smelter returns on all concentrates shipped to independent smelters. (Admissions)

O. That the books and records of defendant correctly show that the royalties payable to the plaintiff on net smelter returns received by defendant, Bradley Mining Company, from independent smelters have been paid to the plaintiff. (Admissions)

P. That at the time of the execution of the contract, December 31, 1941, there were no smelters located at Cascade, Idaho. (Answer and Stipulation)

Q. That, if under the terms of the contract, defendant, Bradley Mining Company is entitled to make any charge or deduction for smelting ores in the Yellow Pine Smelter, the charges and deductions so made by Bradley Mining Company have been proper charges and deductions and all settlements made with the plaintiff have been correct. (Stipulation)

Defendant's Exhibit No. 30—(Continued)

If it is ultimately determined that the net smelter returns provisions of the agreement is applicable to the operations at the Yellow Pine Smelter for ores, concentrates, metals and values taken from the claims described in the agreement, then the settlements made by Bradley have been correct as to the minerals, ores, metals and values processed at the smelter.

R. That there is no dispute as to the meaning and interpretation of the "net mint return" clause of the contract. (Stipulation)

S. That before 1939 and thereafter at all times material to this action, it was the practice and custom in the smelting industry for companies who own and operate smelters to also own and operate mines; that it was likewise the practice and custom in the industry for companies owning mines and also mining smelters to ship their mine products to their own smelters; that it was likewise the practice and custom with respect to owners of smelters and mines to also lease mining properties from other independent owners and send the products extracted therefrom to their own smelters and to settle for the products so shipped on the same basis as such smelting companies would settle with independent or custom shippers; that it was a practice and custom of the trade that where ores treated came from the mines owned by the owners of smelters, or came from mines leased and mined by the smelter owner, or came from independent custom shippers, that the smelting charges and the cost of

Defendant's Exhibit No. 30—(Continued)

transportation of concentrates to the smelter were deducted to arrive at a net amount commonly referred to in the mining and smelting industries as "net smelter returns." (Stipulation)

T. That it is a matter of common knowledge and historically recognized in the mining industry that the milling of ores to reduce such ores to a concentrate form is a part of the mining process and that the smelting of ores is not a part of the mining process. (Stipulation)

IV.

The objections reserved to the facts recited in paragraph III above are as follows:

A. Plaintiff has reserved objection on the ground of materiality or relevancy to the recognized practice and custom in the smelting industry as set forth in III S above.

B. Plaintiff contends that it has reserved objection on the ground of materiality or relevancy with respect to any and all issues raised and to be raised in this action.

V.

The defendant contends that the following issues of fact remain to be litigated upon the trial of this cause, and that the facts and circumstances surrounding the execution of the contract, as set forth in subdivisions B to H, both inclusive, of this paragraph V serve to aid interpretation of the contract.

A. Whether in the computation of royalties to be paid plaintiff on ores smelted at The Yellow Pine Smelter the "net revenue" clause or the "net

Defendant's Exhibit No. 30—(Continued)
smelter return" clause of the contract would apply. (Defendant expects to establish the fact that the "net smelter returns" clause was applicable by the pleadings, stipulations, admissions and legal presumptions, and the sources of its proof will be oral testimony and defendant's exhibits.)

B. The circumstances and reasons for the extinguishment of the 1939 contract and the execution of the contract of December 31, 1941. (Defendant will rely upon the pleadings and legal presumptions and the source of its proof will be by oral testimony and defendant's exhibits.)

C. The conduct of the parties, as bearing on interpretation, after execution of the contract of December 31, 1941, and both before and after construction of The Yellow Pine Smelter. (Defendant will rely upon the pleadings and legal presumptions and the source of its proof will be by oral testimony and defendant's exhibits.)

D. The operation by defendant of the Boise Purification Plant as bearing upon accepted interpretation of the contract. (Defendant expects to establish this fact by the pleadings, by admissions and by legal presumptions and the source of its proof will be oral testimony and defendant's exhibits.)

E. The reasons for the inclusion of the "net revenue" clause in the contracts of 1939 and 1941. (The defendant will expect the fact to be established by the pleadings, admissions and legal presumptions and the source of its proof will be oral

Defendant's Exhibit No. 30—(Continued)

testimony, defendant's identified exhibits, and an exhibit in writing which, after identification, will be offered by the defendant.)

F. The distinction between mining and smelting and that smelting is not considered part of a miner's ordinary treatment processes, and values added by smelting are not values from the mining property. (Defendant expects to establish such facts by stipulations, admissions, judicial notice and legal presumptions, and the manner or source of its proof will be by oral testimony and statute.)

G. That the term "metals produced from the properties" has a distinct application that does not extend to the smelter. (Defendant expects such fact to be established by stipulation, admission, judicial notice and legal presumptions, and the manner and source of its proof will be by oral testimony, defendant's exhibits and statute.)

H. The reason for the inclusion of the word "normal" in the "net smelter returns" clause immediately preceding the words "smelting charges." (Defendant expects this fact to be established by the pleadings, by stipulations, by legal presumptions, and the manner and source of its proof will be by oral testimony, defendant's exhibits and a written exhibit which, when identified, will be offered by defendant.)

The plaintiff contends that the following issues of fact and no others remain to be litigated on the trial of this action:

Defendant's Exhibit No. 30—(Continued)

a. Are royalties on the ores, concentrates, metals and values extracted taken, or produced from the Meadow Creek and Henessy Groups of mining claims and smelted at the Yellow Pine Smelter to be computed and paid in accordance with the "net revenue" provisions contained and defined in the agreement of December 31, 1941?

VI.

The exhibits to be offered at the trial, together with a statement of all admissions by and all issues between the parties with respect thereto are as follows:

A. Defendant's Exhibits marked for identification as Defendant's Exhibits numbered 1 to 22, inclusive may be offered and admitted in evidence subject to exceptions and objections for relevancy and materiality only.

(1) Agreement dated August 5, 1927, between the United Mercury Mines Company and F. W. Bradley, marked as defendant's Exhibit 1 for identification. (No admission by plaintiff as to genuineness or due execution thereof.)

(2) Agreement dated February 1, 1928, between United Mercury Mines and F. W. Bradley, marked as defendant's Exhibit 2 for identification. (No admission by plaintiff as to the genuineness and the due execution thereof.)

(3) Agreement dated August 30, 1929, between United Mercury Mines Company and Yellow Pine Company, marked as defendant's Exhibit 3 for

Defendant's Exhibit No. 30—(Continued)

identification. (No admission by plaintiff as to the genuineness and due execution thereof.)

(4) Agreement dated October 3, 1930, between United Mercury Mines Company and Yellow Pine Company marked defendant's Exhibit 4 for identification. (No admission by plaintiff as to the genuineness and due execution thereof.)

(5) Agreement dated May 16, 1939, between United Mercury Mines Company and Bradley Mining Company marked defendant's Exhibit 5 for identification. (No admission by plaintiff as to the genuineness and due execution thereof.)

(6) Agreement dated July 20, 1950, between United Mercury Mines Company and Oscar W. Worthwine, as parties of the first part, and Bradley Mining Company as party of the second part, marked defendant's exhibit 6 for identification. (No admission by plaintiff as to the genuineness and due execution thereof.)

(7) Agreement dated December 31, 1941, between United Mercury Mines Company and Bradley Mining Company marked defendant's Exhibit 7 for identification. (Admissions by both plaintiff and defendant that defendant's Exhibit 7 is a true and correct copy of the original agreement between the parties dated December 31, 1941)

(8) Letter from United Mercury Mines to its stockholders dated December 20, 1941, marked defendant's Exhibit 8 for identification. (Admission by J. J. Oberbillig to have been sent by him as President of the Company.)

Defendant's Exhibit No. 30—(Continued)

(9) Letter from United Mercury Mines to its stockholders dated June 1, 1948, marked as defendant's Exhibit 9 for identification. (Admitted by J. J. Oberbillig to have been sent by him as President of the Company.)

(10) Statement of the returns of shipment of ore to Sylvania Electric Products Company, marked defendant's Exhibit 10 for identification. (No admission with respect to the exhibit.)

(11) Copy of letter dated April 14, 1948, addressed to J. J. Oberbillig, President, United Mercury Mines, signed by John D. Bradley, marked defendant's Exhibit 11 for identification. (No admission that it is true copy of original.)

(12) Copy of a letter from J. J. Oberbillig to John D. Bradley, dated April 22, 1948, marked defendant's Exhibit 12 for identification. (Admitted by J. J. Oberbillig to be a true copy of a letter written by him on that date and mailed to Bradley.)

(13) Schedule.

Summary of Gold Concentrate settlement sheets. Y.P.M. - Y.P.S.

(14) Schedule.

Summary of Antimony Concentrate settlement sheets. U.P.M. - Y.P.S.

(15) Schedule.

Detail of Royalty Paid from beginning of smelter operations to December 31, 1953.

(16) Schedule.

Yellow Pine Smelter illustrative Royalty Calculations. Sheet A.

Defendant's Exhibit No. 30—(Continued)

(Schedules marked defendant's Exhibits 13, 14, 15 and 16 have been identified and by stipulation agreed that they are correct copies taken from the original records of Bradley Mining Company—objection reserved as to admissibility.)

(17) Letter dated November 17, 1941, from Oscar W. Worthwine to Bradley Mining Company, marked defendant's Exhibit 17 for identification. (Admission as to genuineness—objection reserved as to admissibility.)

(18) Letter dated November 14, 1941, from Oscar W. Worthwine to John D. Bradley, marked defendant's Exhibit 18 for identification. (Admission as to genuineness—objection reserved as to admissibility.)

(19) Letter from J. J. Oberbillig to John D. Bradley, dated November 17, 1941, marked defendant's Exhibit 19 for identification. (Admission as to genuineness—objection reserved as to admissibility)

(20) Telegram from Oscar W. Worthwine to Bradley Mining Company, dated December 11, 1941, marked defendant's Exhibit 20 for identification. (Admission as to genuineness—objection reserved as to admissibility.)

(21) Letter dated December 30, 1941, from Oscar W. Worthwine to Bradley Mining Company, marked defendant's Exhibit 21 for identification. (Admission as to genuineness—objection reserved as to admissibility.)

Defendant's Exhibit No. 30—(Continued)

(22) Letter dated December 30, 1941, from Oscar W. Worthwine to Bradley Mining Company, marked defendant's Exhibit 22 for identification. (Admission as to genuineness — objection reserved as to admissibility.)

(23) Portion of rough draft of 1939 contract between plaintiff and defendant not yet identified, to be offered by the defendant as defendant's Exhibit 23, subject to objections as to relevancy and materiality.

B. Plaintiff's exhibits will consist of the agreement of December 31, 1941, all Interrogatories served and the Answers thereto, now on file herein, all Requests for Admissions and the Answers thereto, now on file herein, and writings to explain, clarify or rebut the contents of defendant's Exhibits above identified, subject to defendant's exceptions and objections for relevancy and materiality only.

VII.

The defendant contends that following issues of law, and no others, remain to be litigated upon the trial of this cause:

a. The interpretation of the contract of December 31, 1941, particularly to determine whether defendant was properly entitled to compute the royalties payable to plaintiff on ores produced from defendant's property and processed in The Yellow Pine Smelter on the basis of the "net smelter returns" clause, or whether the same should have been computed on the "net revenue" clause.

Defendant's Exhibit No. 30—(Continued)

VIII.

Expert witnesses are limited to three on each side, subject to revision by the Court.

IX.

The case is hereby set for non-jury trial (estimated to require three (3) days) at 10:00 o'clock a.m. on March 19, 1957.

X.

The foregoing admissions of fact having been made by the parties, and the parties having agreed to the foregoing statement of the issues of fact remaining to be litigated and the contention of the parties with respect thereto and with respect to the issues of law, this Order shall supplement the pleading and govern the course of the trial of this cause, unless modified to prevent manifest injustice.

Dated this 11th day of March, 1957.

/s/ WM. C. MATHES,
United States District Judge.

Approved as to form and content:

/s/ PAUL S. BOYD,
/s/ DALE CLEMONS,
Attorneys for Plaintiff,
Residence: Boise, Idaho.

/s/ RALPH R. BRESHEARS,
Of Counsel for Defendant,
Residence: Boise, Idaho.

[Endorsed]: Filed March 19, 1957.

PLAINTIFF'S EXHIBIT No. 31

[Letterhead of Bradley Mining Co.]

December 2, 1948

Mr. John J. Oberbillig, President,
United Mercury Mines Co.,
256 Sonna Building, Boise, Idaho.

Dear John:

Subject: United Mercury Mines Royalty Situation After Smelter Commences Operation

Referring to our conversations in Boise last week in company with Messrs. Driscoll, Worthwine, and Davis, I wish to advise you that I have given continued thought to the matter of the proper method of determining the point at which the 5% royalty should apply after our smelter commences operations in July or August of next year. In reviewing this situation I continually return to the premise that the gross yield from the sale of products coming out of the smelter is allocable to three principal categories:

(a) the gross income which is derived from mining;

(b) the gross income which is derived from ore dressing and concentration;

(c) the gross income which is derived from roasting and smelting operations.

Each of these activities is entitled to a reimbursement of its cost, including depreciation on the equipment and an annual remuneration on the investment contributing to the profits.

Plaintiff's Exhibit No. 31—(Continued)

The Bureau of Internal Revenue allocates gross income into only two categories:—gross income from mining, and gross income from roasting and smelting. The Income Tax Law and Regulations classify all ore dressing and concentration as “mining operations”.

It has been my suggestion that we agree to base the royalty upon the fair market value of the concentrates at the mouth of the roaster for a period of three years beyond January 1, 1950, and to include that portion of 1949 during which the smelter will operate. Truck and/or rail freight to a competing smelter will not be deducted in determining the market value of the concentrates at the mouth of the roaster.

On October 1, 1953, i.e., three months prior to the termination of such an agreement, we should review the situation and then negotiate a new formula for valuation of the concentrates in the light of the facts then existing. At that time we would ask for bids on concentrates being currently produced, and strive for an agreement which would be followed for the ensuing three-year period from January 1, 1954 to December 31, 1956. We could agree now with respect to the valuation of concentrates for that period on a formula which might be applied in case we could not secure bona fide bids for our concentrates at that time.

I suggest the following formula to be used in lieu thereof if these circumstances exist:

Reduce the proceeds from the sale of the prod-

Plaintiff's Exhibit No. 31—(Continued)

ucts coming from the smelter by the operating costs necessary and incidental to the production of the products in the smelter and roaster.

Reduce this balance by a reasonable depreciation on the smelter and roaster and the other tangible property necessary and incidental to the smelting operations.

Then reduce the balance by a remuneration on the investment in the smelter and the roaster at a percentage which will approximate the yield made on investments by comparable smelters.

This formula, of course, would not be used by us if we could procure bona fide bids for the concentrates from custom smelters f.o.b. smelters contacted.

I propose as an amendment the following:

It is understood and agreed that the basis for United Mercury Mines royalty payments from the commencement of the smelter until December 31, 1953, will be the highest amount that would be received if concentrates were shipped under present prevailing contracts. These concentrates, we now anticipate, will analyze as follows:

Gold concentrate:

2.3	ozs.	gold
3.6	ozs.	silver
4-7	%	antimony
7	%	arsenic
35	%	iron
37	%	sulphur
10	%	SiO ₂

Plaintiff's Exhibit No. 31—(Continued)

Antimony concentrate:

0.75 ozs. gold

16. ozs. silver

42 % antimony

13 % iron

3.4 % arsenic

20 % sulphur

12 % SiO_2

For antimony concentrate the highest value calculated from the following two contracts will prevail:

1. Harshaw Chemical Co.
2. Bunker Hill & Sullivan.

For the gold concentrate the highest value calculated from the following contracts will prevail:

1. A. S. & R. Co. (a) Selby Smelter. (b) Garfield Smelter.
2. U. S. Smelting Refining & Mining Co.—Midvale plant.

Provided you agree to this procedure, we will submit copies of the above-mentioned contracts for your study.

Under the proposed new arrangement (effective from the commencement of smelter operations to December 31, 1953) we would determine the tonnage and contents of concentrates produced in the Yellow Pine Mine concentrator from ores extracted from the Yellow Pine Mine. We would combine these figures into a statement for you on which they would be tabulated, totaled, and the to-be-agreed-upon smelter formula applied to determine the

Plaintiff's Exhibit No. 31—(Continued)
value of the concentrator output subject to royalty. The statement and check for the royalty would be submitted to you by the 20th of the second succeeding month following the month of production. This timing would approximate our present arrangement, as about one month is now required for shipment and settlement.

As you will note, copies of this letter are being mailed to Lynn Driscoll and Oscar Worthwine—I trust you will get together there for a discussion re. this matter at an early date, so that by the time of my Boise return (approximately December 13) we can have a general conference.

With kindest regards, I am

Sincerely yours,

/s/ John D. Bradley,
Executive Vice President.

JDB:MM—cc. Lynn Driscoll, O. W. Worthwine.

DEFENDANT'S EXHIBIT No. 32

[Letterhead of Bradley Mining Co.]

March 31, 1948

Mr. John J. Oberbillig, President,
United Mercury Mines Co.,
256 Sonna Building, Boise, Idaho.

Dear John:

As Harold Bailey and I explained to you on March 12, 1948 in your office, we are planning on

Defendant's Exhibit No. 32—(Continued)

erecting at Stibnite a smelter for the local reduction of our antimony concentrates — our present plans also include locally reducing our gold concentrates in the future.

Although I am positive that you fully appreciate the importance of such a move, still I am listing below the benefits of a smelter to the Yellow Pine Mining District as we see them at present.

1. Longer life for Yellow Pine Mine.

Upgrading of marginal ore bodies owing to greater metal recoveries and payments will add longer life to the Yellow Pine Mine. At the present time we have approximately $11\frac{1}{2}$ million tons of low-grade antimony-gold ore which can only be made profitable with a local smelter—undoubtedly, large additional tonnages of this type of material will be developed as we continue our drilling and other exploration programs.

2. Larger metal payments.

Under the present program of shipping raw concentrates, there is no pay for gold and silver in the antimony concentrates; and in the instance of the gold concentrates, there is little and sometimes no pay for the antimony contained in these concentrates — this situation will be corrected by the smelter installation.

3. Greater metal recoveries.

In having to make special grades of concentrates for the marketing of raw antimony concentrates, there is a larger concentrating loss than will be the case when only one grade antimony concentrate

Defendant's Exhibit No. 32—(Continued)
need be produced for the local smelter.

4. Prospects in area will have much better chance of becoming productive.

5. Prospecting in area will be stimulated.

6. Many benefits to National Defense program.

(a) Greater antimony metal recovery at less material and manpower cost.

(b) Making commercial large tonnage of low-grade antimony ore.

(c) Stimulus to antimony prospecting and mine development in entire Northwest.

(d) Elimination of heavy trucking operations which consume large quantities of critical materials.

(e) Making available railroad cars which are now tied up hauling antimony concentrates to various parts of the United States.

It appears to us that with your foresight and great faith in the Yellow Pine Mining District you are as anxious as we to see the smelter completed at as early a date as possible. In fact, you raised the question at our March 12, 1948 meeting why we had not taken earlier action on this important matter. My reply to this, as you will recall, was that we not only had to eliminate other likely possibilities for local reduction before deciding on the present pyrometallurgical plant, but that we also had to study and analyze the demand situation along with the ability of other countries to produce in competition with us. We have not been able to eliminate completely all the questions that occur to us re. the latter, but after going into the matter with the Na-

Defendant's Exhibit No. 32—(Continued)

tional Lead Company (which is this country's largest antimony consumer), we have developed sufficient faith to take the deep step. Another main reason for our hesitancy, of course, has been the rather limited tonnage of antimony ore developed in the past. Our reserves of gold ore are far in excess of our antimony ore reserves, but we believe we now have enough antimony ore to pay for the smelter, and also have faith that we will discover more ore in the near future. As you know, we are now carrying on two major development campaigns in the Meadow Creek and Clark Tunnel areas.

In view of the foregoing described smelter program, there is need for giving early consideration to altering our agreement.

According to the present Bradley Mining Co.-United Mercury Mines Co. contract, "normal smelting charges" are to be deducted in arriving at "net smelter returns". "Normal smelter charges", as you know, are comprised not only of treatment charges but also metal and quotational gains. In fact, in the case of our antimony shipments the "normal smelting charges" are entirely quotational gains.

I believe you will agree with us that to arrive at "normal smelting charges" for our several different types of concentrates in the case of a local smelter can prove most complex over the ensuing years. Accordingly, I am proposing a simplified procedure for locally reduced concentrates—such procedure to be equivalent to the royalty you now receive on the

Defendant's Exhibit No. 32—(Continued)
present 5% basis when it is applied to the shipment of raw concentrates.

Although the following calculations show a variance for the equivalent royalty in the instance of sales of locally reduced products from 2.30% to 2.58%, we have proposed that the rate for such products be set at 2.75%.

Sb Concentrate:

1. Actual 1947 net smelter returns for all Sb concentrate including Bunker Hill Smelter	\$1,666,882
Less Hauling Allowance	33,583
Subject to Royalty	\$1,633,299
Royalty @ 5%	\$ 81,665
2. 1947 net smelter returns, had all Sb concentrate except that to Bunker Hill Smelter gone to Harshaw Chemical Co. at December price and freight, would have been	\$1,407,670
Bunker Hill Smelter	302,835
	\$1,710,505
Less Hauling Allowance	33,583
Subject to Royalty	\$1,676,922
Royalty @ 5%	\$ 83,846
3. 1947 net smelter returns, had all Sb concentrate except that to Bunker Hill Smelter gone to Harshaw Chemical Co. at April 1948 price and freight, would have been	\$1,509,771
Bunker Hill Smelter	302,835
	\$1,812,606

Defendant's Exhibit No. 32—(Continued)

Less Hauling Allowance	33,583
Subject to Royalty	\$1,779,023
Royalty @ 5%	\$ 88,951

Assuming that a local smelter would recover 100% of the metals contained in this concentrate and that they could be sold at prevailing prices, the dollar recovery would be:

Au 9,355 oz. @ \$34	\$ 318,070
Ag 201,967 oz. @ 90c-5%	172,682
Sb 9,588,750 lbs. @ 32c	3,068,400
	<u>\$3,559,152</u>

Equivalent Royalty to No. 1 above	2.30%
Equivalent Royalty to No. 2 above	2.36%
Equivalent Royalty to No. 3 above	2.50%

Au (Regular) Concentrate:

Net smelter returns (actual) (United States Smelting Refining & Mining Co.)	\$ 481,008
Less additional freight now in effect @ 20%	9,375
	<u>\$ 471,633</u>
Less Hauling Allowance (7,257 W.T.)	18,143
Subject to Royalty	\$ 453,490
Royalty @ 5%	<u>\$ 22,675</u>

Note: The above \$481,008 net smelter returns actually includes Sb price adjustment of approximately \$3,800 a/c 1946 shipments. If this were removed the equivalent royalty given below would be 2.56%.

Assuming local smelter, 100% recoveries, etc. (as above), the dollar recovery would be:

Au 14,323 oz. @ \$34	\$ 486,982
Ag 39,900 oz. @ 90c-5%	34,115

446 *United Mercury Mines Company vs.*

Defendant's Exhibit No. 32—(Continued)

Sb 1,118,968 lbs. @ 32c	358,070
	<hr/>
	\$ 879,167
	<hr/>
Equivalent Royalty	2.58%
	<hr/>
Au (No. 2) Concentrate:	
Net smelter returns (actual) (American Smelting & Refining Co.)	\$ 179,327
Less additional freight now in effect @ 20%	4,088
	<hr/>
	\$ 175,239
Less Hauling Allowance (3,137 W.T.)	7,843
	<hr/>
Subject to Royalty	\$ 167,396
	<hr/>
Royalty @ 5%	\$ 8,370
	<hr/>
Assuming local smelter, 100% recoveries, etc. (as above), the dollar recovery would be:	
Au 6,933 oz. @ \$34	\$ 235,722
Ag 11,826 oz. @ 90c-5%	10,111
Sb 322,328 lbs. @ 32c	103,145
	<hr/>
	\$ 348,978
	<hr/>
Equivalent Royalty	2.40%
	<hr/>

Please give the foregoing your early and serious consideration so that we can discuss it in Boise later this month.

With kindest regards, I am

Sincerely yours,

/s/ John

John D. Bradley,

Executive Vice President.

JDB:MM—cc: OWW

[Endorsed]: No. 15652. United States Court of Appeals for the Ninth Circuit. United Mercury Mines Company, a corporation, Appellant, vs. Bradley Mining Company, a corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the District of Idaho, Southern Division.

Filed July 31, 1957.

Docketed: August 5, 1957.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals for the Ninth Circuit

No. 15652

UNITED MERCURY MINES COMPANY, a corporation, Appellant,

vs.

BRADLEY MINING COMPANY, a corporation, Appellee.

STATEMENT OF POINTS

The appellant submits the following statement of points on which it will rely in this appeal as follows:

I.

The court erred in making the following findings of fact:

- (a) Paragraph XIX.
- (b) Paragraph XXI.
- (c) Paragraph XXII.
- (d) Paragraph XXIII.
- (e) Paragraph XXIV.
- (f) Paragraph XXV.
- (g) Paragraph XXVI.

(h) That portion of Paragraph XXVII, as follows: "and that in itself would be a construction contrary to the purpose of the contract and contrary to plaintiff's avowed purpose at the time the contract was executed."

(i) That portion of Paragraph XXVIII, as follows: "and in that contemplation the parties inserted in the contract the following provision: 'Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.'"

- (j) Paragraph XXIX.
- (k) Paragraph XXXI.
- (l) Paragraph XXXIII.
- (m) Paragraph XXXIV.
- (n) Paragraph XXXV.
- (o) Paragraph XXXVI.
- (p) Paragraph XXXVII.
- (q) Paragraph XXXVIII.

(r) Paragraph XXXIX.

(s) Paragraph XL.

(t) Paragraph XLI.

II.

The Court erred in concluding:

(a) Under paragraph II of its conclusions of law that the proper and legal method for determining the amount of royalty due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941 for minerals, ores, metals and values extracted from the mining claims described therein and smelted at the Yellow Pine smelter of the defendant is by the use of "net smelter returns" provision as defined in the contract and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of saleable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by the defendant at the Yellow Pine Smelter.

(b) Under paragraph III of its conclusions of law that the defendant does not owe plaintiff anything by way of royalties, or otherwise, for or on account of any ores, concentrates, metals or values taken from the mining claims described in said contract and processed at the Yellow Pine smelter.

III.

The Court erred in adjudging:

(a) In Paragraph I. of its Judgment, that the

proper and legal method for determining the amount of royalties due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941 for minerals, ores, metals or values extracted from the mining claims described therein and smelted at the Yellow Pine smelter of the defendant is by the use of "net smelter returns" provision as defined in the contract and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of saleable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by defendant at the Yellow Pine smelter.

(b) In Paragraph II. of its Judgment, that the defendant is not indebted to the plaintiff, and that the plaintiff is not entitled to recover from the defendant any monies by way of royalty, or otherwise, for and on account of any ores, concentrates, metals or values taken from the mining claims described in said "Conveyance, Royalty Agreement and Option" and processed at Yellow Pine smelter.

Dated this 13th day of August, 1957.

PAUL S. BOYD,
E. H. CASTERLIN,
DALE CLEMONS,

/s/ By DALE CLEMONS,

Attorneys for Appellant.

Acknowledgment of Service Attached.

[Endorsed]: Filed August 13, 1957. Paul P. O'Brien, Clerk.

IN THE
United States
Court of Appeals
For the Ninth Circuit

UNITED MERCURY MINES COMPANY,
Appellant,
vs.
BRADLEY MINING COMPANY,
Appellee.

REPLY BRIEF OF APPELLANT

*Appeal from the United States District Court
For the District of Idaho, Southern Division*

PAUL S. BOYD,
P.O. Box 2084, Boise, Idaho

E. H. CASTERLIN,
P.O. Box 1384, Pocatello, Idaho

DALE CLEMONS,
Idaho Building, Boise, Idaho,
Attorneys for Appellants.

FILED

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Attorneys for Appellants.



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IN THE
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UNITED MERCURY MINES COMPANY,
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REPLY BRIEF OF APPELLANT

*Appeal from the United States District Court
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ARGUMENT

United, in reply to Bradley's brief, sets forth herein its position and reply.

The decision of this Court of May 15, 1956, United Mercury Mines Company v. Bradley Mining Company, 233 F. 2d 205, states at page 207 with reference to the "net smelter returns" clause:

"By its terms this clause is limited to situations where amounts are received (by Bradley) from (outside) smelters."

Thus, under the facts in our case, the net smelter returns clause does not apply to the Yellow Pine Smelter operations.

The sole issue is,—does the “net revenue” clause apply to the operations at the Yellow Pine Smelter. This Court said in the same decision at the same page:

“We see no reason why, as a matter of law, the ‘net revenue’ could not be controlling.”

The question of law is thus eliminated and there is left the problem to determine if, as a matter of fact, the “net revenue” clause applies.

If, as a matter of fact, the “net revenue” clause does not apply to the operations at the Yellow Pine Smelter, then the parties have been operating outside the terms of their contract. Generally, the various provisions of a contract must be so construed, if possible, to give force and effect to every part thereof. *Wright vs. Village of Wilder*, 117 P. (2) 1002, 63 Ida. 122.

A contract must be given effect according to its terms whenever possible and courts cannot substitute or write a new contract for the parties. *Durant v. Snyder*, 151 P. (2) 776, 65 Ida. 678.

Where the language of a contract is clear, courts give effect to the language employed according to its ordinary meaning. *Durant v. Snyder*, *supra*.

It must be remembered that prior to December 31, 1941, the parties were lessor and lessee. Whatever work the lessee did in mining the ore was with reference to the lessor's property and was governed

by the terms of the lease. Whatever was done with the ore after it was mined was also the subject matter of the lease in which the parties generally agreed that the ore was to be shipped to a smelter in the owner's name and the net smelter returns divided in accordance with the agreement, but sometimes agreed that the ore was to be otherwise treated and the values sold in the name of the owner and the proceeds divided per agreement. The lessor (owner) had control of its own property until the time for the division of the returns from the smelter or from an ore buyer in the market.

After December 31, 1941, the relation was that of owner and unpaid seller, Bradley being the owner and United the unpaid seller. The owner agreed to pay the purchase price of the property (claims and values of every kind therein) in a particular manner, to-wit:—by turning over to the seller, whenever it was received by the owner, five percent of the money from the mint, from the smelter, or from any other purchaser of the “concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho” (R 17) and, under certain conditions certain other costs.

After December 31, 1941, whatever Bradley did with the ores from the claims was with respect to its *own property* and without any control of the seller. Bradley, as owner, elected what to do with the values and when and to whom to sell the same; they were Bradley's property, subject to Bradley's management and control in every respect.

All that Bradley, owner, was required to do was to pay over to United 5% of its receipts from the sale of values to a smelter or to a "purchaser."

Bradley, in its brief, argues at great length concerning the difference between a "mining process" and a "smelting process." United contends that this is immaterial for the following reasons: First, Bradley was operating on its own values, for its own use and according to its independent judgment. Second, Bradley agreed to pay, when the concentrates were not sent to an independent smelter, 5% of whatever it received from the sale of values "shipped, taken or produced from said properties" regardless of the state of refinement. Third, the parties agreed to all deductions that were to be taken from the "amounts received" and if there were to be other deductions the same would have been included with the enumerated deductions (R 17-18). Fourth, the erection of a smelter or other reduction works was discussed and the parties finally decided to cover the situation with respect to trucking costs by the language which appears in the contract (R 18). Fifth, the officers of the respective parties were experienced mining men and operators and it must be assumed or inferred that they knew at all times the practice of mining, smelting and metallurgy.

The difference between mining operations and smelting operations, as such, is immaterial in computing 5% of *money received* from the purchaser of any values which found their origin in the claims, less the deductions enumerated in the contract as

agreed upon, regardless of whether the purchaser was a smelter or a person other than a smelter.

The language of the agreement is plain, clear and unambiguous with reference to sales to a smelter or to a purchaser. The plan conceived by Bradley for paying royalties on concentrates processed at the Yellow Pine Smelter is foreign to the terms of the agreement in that it is not based on "any amount received," but is based on a hypothetical situation which may vary from day to day, leaving the day on which the market value is taken up to Bradley. Bradley's method of computing royalty on concentrates smelted at the Yellow Pine Smelter continues the ownership of the values in Bradley subject to a rising or falling market. Contrary to the terms of the contract, this construction of Bradley forces United to share in costs of processing the values exclusively owned by Bradley. In other words, United is forced to deduct from money received from the sale of values in whatever state they may be found, items that are not provided for in the agreement. Thus, Bradley sells its smelted product to a "purchaser" and then deducts items that are not specified in the contract.

Bradley still insists that the "net smelter returns" clause applies regardless of the decision of this Court, regardless of whether the concentrates are sold to an outside smelter, and Bradley's entire offer of testimony was for the sole and admitted purpose of establishing the applicability of the "net smelter returns" provision of the contract to the Yellow Pine Smelter.

Bradley's brief says at page 7:—

“The question then is, shall United get the same royalty when the concentrates go through a smelter owned by Bradley on the premises—as if they went through an independently owned smelter—or is United to get a greater royalty merely because the smelter is owned by Bradley.”

This is not the question.

The question is: Shall Bradley pay a royalty on the amount received from a *purchaser* of values processed at the Yellow Pine Smelter? This has been United's position from December 31, 1941. In the pre-trial conference order United there stated its position as to the issue “are royalties on ores, concentrates, metals and values extracted, taken, or produced from the Meadow Creek and Hennessy Group of mining claims and smelted at the Yellow Pine Smelter to be computed and paid in accordance with the “net revenue” provisions contained and defined in the agreement of December 31, 1941 (R. 430)?

If Bradley elects to further reduce its concentrates, no matter to what extent, before there is a sale, then it profits by 95% of the increase and United gets no more than it is entitled to have under the agreement. To United it seems that Bradley's position is to profit by not paying the full purchase price of the property according to its promise, and that paying according to the terms of the agreement cannot be a “windfall.”

The reason for the inclusion of the “net revenue” clause is clear from the record. As early as 1937 it

was expected that the claims would produce values other than antimony and gold which are processed by smelting (R. 103). Before 1939 the provisions of "net revenue" came into being and was included in the 1939 contract after having been fully discussed by the parties (R 105, 113). "Net revenue" is an expression not common in the mining industry and is peculiar to the contract of December 31, 1941 (R 105, 106).

Therefore, there is no precedent in the mining industry which will help explain the purpose of the "net revenue" clause. The contract of December 31, 1941 must stand by itself as no instance where this term has been used by others or has been interpreted by usage or by the courts has been pointed out.

"We were hunting for a clause that would cover,—the net mint returns was in there, and we were hunting for a clause that would cover these other possibilities. Mr. Worthwine had one suggestion in there and *I changed it with the objective of submitting it to for his approval and Mr. Oberbillig's approval*, a catchall clause that would cover all of these other things that we didn't know just what might be. We knew of several, that the quicksilver didn't come under the net mint and technically it didn't come under net smelter, so that was the course of the conversation, and from that conversation the net revenue clause was picked up." (R 122) (Emphasis supplied.)

Not only was the "net revenue" clause prepared and submitted by Bradley, and the defendant testified

that the "net revenue" clause was devised and included in the agreement as a catchall to cover "the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties" in the event the "net smelter returns" or "net mint" clause is not applicable.

Because the concentrates treated at the Yellow Pine Smelter do not fall within the provisions of the "net smelter returns" provision and because the processed or smelted values are eventually sold to a "purchaser" the "net revenue" provision, not being impossible of application, must be the basis of royalty computations. The record clearly indicates that both parties admit that they were operating under the 1941 contract and prior to the construction of the Yellow Pine Smelter there was no trouble between the parties as to payment of royalties. It was after the construction of the Yellow Pine Smelter that Bradley, on ores handled at the Yellow Pine Smelter, claimed that the basis of payment of royalty was the "net smelter" provision and United claimed that the basis of payment was the "net revenue" provision and that it could be and should be adopted as the basis of payment for royalties on values smelted at the Yellow Pine Smelter and ultimately sold at the mint.

Bear in mind that the December 31, 1941 contract was to continue for 999 years. It must be assumed that both parties intended to operate under that agreement as the same has never been amended by mutual agreement of the parties. Now, with respect

to the operations at the Yellow Pine Smelter, United insists that Bradley comply with the plain, clear and unambiguous terms thereof. Bradley insists that it may amend the agreement by smelting concentrates at its own smelter on the claims and paying royalties on the concentrates "on the basis of past practices of antimony shipments to outside smelters." (R 171; Brief page 19.) This "basis" is rejected by United as not having been the agreement.

The various bases of settlement were all subjects of negotiations before the 1941 contract was drafted and the same were intended to be covered and were covered in the agreement. Certainly, the subject matter of this controversy, to-wit: the method of computing royalties, is mentioned, covered and dealt with in the agreement of 1941, and, therefore, the writing was intended to represent all the transactions on this issue.

Bradley, in its brief, stresses the purification plant and United's failure to object to the payment of royalties between the time the smelter started operations in 1949 and 1951 as indicating a mutual construction of the contract between the parties permitting "net smelter" to be the basis for computing royalties on concentrates passing through the Yellow Pine Smelter. A letter of December 2, 1948 from Bradley to United concerning the "United Mercury Mines Royalty Situation After Smelter Commences Operation" (R 436-440) was written prior to the installation of the Yellow Pine Smelter and at a time when discussions were being had between the parties with reference to the Yellow Pine Smelter. In this

letter (Exhibit 31, R 436-440) Bradley proposes that the contract be amended to provide:

“That the basis for United Mercury Mines royalty payments from the commencement of the smelter until December 31, 1953 will be the highest amount that would be received if concentrates were shipped under present prevailing contracts.”

This is “net smelter” according to the very definition given it by Bradley and was the mode of accounting used by Bradley after the smelter was constructed. Had the “net smelter” provision of the contract as originally drawn covered this situation, there would have been no occasion for this amendment. This proposal was rejected by United and the contract was never amended. This letter (Ex. 31) flatly and completely contradicts the testimony of the witness John Bradley that there was an objection by United to the computation of royalties as made by Bradley on products passing through the Yellow Pine Smelter. This, likewise, refutes any implication that the acceptance of royalties by United from Bradley on concentrates passing through the purification plant was any interpretation or waiver of any of United’s rights under the contract.

Prior to 1941 the possibility of a smelter erected by Bradley was discussed. (R 131-134; 160-165.) At the same time the “net revenue” and “net smelter returns” clauses of the agreement were discussed. If it had been intended that the “net smelter returns” provision was to apply to any smelter built by Bradley, the language defining “net smelter returns”

would not have been limited to "the amount received" from a sale to a smelter, and would have said in simple terms that the same provision would apply to any smelter built by Bradley. It must be assumed, under the circumstances, that one of the methods of computing royalty would apply to a Bradley owned smelter and it is submitted that the method applicable is the "net revenue" provision.

Whatever may be the method of intra company accounting that custom existed prior to the agreement of 1941 and was known to Bradley who drafted the "net revenue" clause and was known to him when he testified that the "net revenue" clause was a catch-all, the effect of which would be to cover all instances not included in the "net smelter returns" provision. That custom cannot, therefore, be used by Bradley to explain what his plain language means unless there was some agreement to that effect. What one party to an agreement understands is immaterial, in the absence of fraud; the question is what did both parties agree to.

The trial court did comment to the effect that if Bradley could not deduct its smelting charges, it would result in a substantial increase in the royalty paid United. (R 251) This assumes that the "net smelter" clause is the proper basis for computing royalties and does not take into consideration the following. In smelter charges is the item of depreciation and such a deduction results in United contributing to the costs of constructing the Bradley smelter. When Bradley sells the smelted product it gets a price greater than the value of the concentrates

plus costs of smelting. The result is that Bradley collects the costs of smelting from two sources and included in the sale of the end product is a profit, 5% of which should go to United under the "net revenue" clause. Bradley is profiting unduly and United is losing a substantial portion of the sale price of the property.

There is no question but that the smelting process adds value to a crude ore. But to whose ore? In our case to the ore of Bradley, 95% of which is to its profit and 5% of which is applied to the purchase price of the mining property according to the terms of the contract. If the parties had agreed to pay and accept for the property 5% of the value of the crude ore or concentrates, they could easily have said so. But they did not. On the contrary, it was agreed to pay and accept 5% of the value of the ores in their crude condition (as in the event of sale to a purchaser), in their concentrated form (as when sold to an outside smelter), or in whatsoever condition they may be (as when sold to a purchaser). It must always be remembered that the ore remained the property of Bradley until sold and that Bradley was the sole judge of when the ore would be sold and the condition in which it would be when sold; and Bradley would take 95% of the money received and United 5% thereof, when the price was paid. And in this connection it makes no difference whether "roasting, thermal or electric smelting or refining" is or is not a "mining process" or a "metallurgical" process. That distinction cannot alter the terms of

the contract except upon mutual agreement, which is lacking.

The word "normal" when used in the expression of "normal smelting charges" applies and is material only when the concentrates are sold to an outside smelter. Its definition has no place in determining if the "net revenue" clause does or does not apply here.

The expression "produced from said properties" does not have a strained construction. It is merely a limitation on what "concentrates, ores, metals or values" are affected by the definitions of "net revenue." Before the "net revenue" is to be used as the basis for computing royalties, it must first be determined if the source of the revenue comes from the sale of "concentrates, ores, metals or values" which find their origin in the particular claims.

The trial Court made its own definition of "produced from said properties" and held that it means or is limited to "Marketing ore, concentrates and values *direct to third persons from the mine, after the mining process has been completed.*" We now ask, where in the definition of net revenue is to be found any language which includes, by reference or inference, values "direct to third persons from the mine" or is limited by that phrase? We ask where in the definition is there any requirement or limitation, by reference or inference, that the "net revenue" clause ceases to operate with the cessation of mining process? The time when royalties is to be computed is fixed by the parties to the time when "money is paid by any purchaser" and the royalty is to be paid out of that particular fund.

If the position of the trial Court is correct, then no money is owed for royalties until there has been a sale and if the sale is after treatment of the ores following mining processes, then from the "money paid" must be deducted other undeterminate items to arrive at the amount of the total payment representing the values at the moment mining processes cease. This is a complication no one anticipated or provided for. It is an impractical, complicated and uncertain method not contemplated by either of the parties at the inception of the contract and would have the effect of replacing the contract of December 31, 1941 by the opinion of the court. This complication was recognized by Bradley as early as April of 1948 when in its letter to United (R 382-387, Ex. 11), wherein Bradley sought to amend the contract by providing for a 2.75% royalty for the end product from the smelter. This offer United rejected and elected to stand on the provisions of the contract.

SUMMARY

The contract of December 31, 1941 is a simple, plain and unambiguous contract. The parties have by clear and unambiguous language spelled out the purchase price to be paid by Bradley to United for this property. Plainly, it is 5% of all monies received by Bradley from any products arising from these mining claims. Bradley has attempted to make this contract seem complicated, primarily because it is financially advantageous to Bradley. United is to be paid only when Bradley receives money from the sale of the products of these properties. Until there

is a sale, there is no royalty due and when there is a sale Bradley owes United 5% of the proceeds less the conceded deductions for freight and marketing as spelled out in the contract.

In conclusion, United submits that the trial court erred in admitting any evidence on the applicability of "net smelter" returns, in holding that "net smelter" returns applied, and erred in not holding that under the evidence and decision of this court that the "net revenue" provision applied as a matter of law.

Respectfully submitted,

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No. 15652

In the

United States Court of Appeals

For the Ninth Circuit

UNITED MERCURY MINES COMPANY, a corporation

Appellant,

vs.

BRADLEY MINING COMPANY, a corporation

Appellee.

BRIEF OF APPELLEE

Appeal from the United States District Court for the District of Idaho,
Southern Division

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BRIEF OF APPELLEE

Appeal from the United States District Court for the District of Idaho,
Southern Division

Summary Statement of the Case

NATURE OF APPEAL

This case involves the interpretation of a written agreement entered into by appellant (United herein) and appellee (Bradley herein) on December 31, 1941 (R. 12 ff). The agreement covers certain mining claims in the State of Idaho. The dispute concerns the manner of computing royalties on minerals and ores extracted from the mining claims.¹

(1) Time to file this reply brief was extended to December 20, 1957 by order of this Court.

All emphasis in quotations has been added unless otherwise indicated.

A summary judgment in favor of Bradley was reversed by this Court and the case was remanded to the District Court for further hearing on the merits.² The pre-trial conference and trial were held before District Judge William C. Mathes at Boise, Idaho.

The District Court determined that the December 31, 1941 contract was unclear (R. 98, 99, 242).³ Testimony was received, *all of which was uncontradicted*, as to extrinsic evidence bearing upon the meaning of the contract—the surrounding facts and circumstances, mining industry custom and usage, and conduct of the parties. United rested its case after the introduction of certain documents (R. 91), and produced no witness or testimony in support of its interpretation of the agreement or in rebuttal of Bradley's evidence. Judgment was rendered for Bradley. We respectfully submit that the judgment below is fully supported by the record and should be affirmed.

THE ISSUE OF CONTRACT CONSTRUCTION

Bradley had been mining United's claims since 1927 under a succession of royalty agreements. A May 16, 1939 agreement was changed to a conveyance on December 31, 1941 of the claims to Bradley.

As consideration, Bradley promised to pay five per cent (5%)—a lower royalty than the 1939 contract—for 999 years

“on all net smelter returns, net revenue, and net mint returns, as defined herein, upon and for all minerals, ores, metals or values, of any and every kind and character, mined, extracted or taken from the above

(2) *United Mercury Mines Company v. Bradley Mining Company*, 233 F.2d 205.

(3) Judge Mathes' comments after trial and argument of counsel (R. 242-253) are set forth in the Appendix to this brief.

described mining claims, or any part thereof, or from any lands, grounds or claims, lodes or deposits, within the exterior boundaries of said groups of claims * * * (R. 15)

The 1941 agreement royalty provisions are referred to as "net smelter returns", "net revenue" (or market) and "net mint returns"—**also** as "smelter, *market*, and mint" (R. 15-18). The provisions *at issue* are "net smelter returns" and "net revenue"—*not* the "net mint returns" clause.

Without some background of the mining and smelting industries, these terms may have little reality. These observations are based on the uncontradicted record.

Mining Process—Smelting Process:

One basic (and stipulated) fact is that "mining" is recognized to be different from "smelting" or the smelting process. A mine operator extracts ores from the ground and customarily crushes and treats them at the mine in a mill (concentrator). This "ordinary mining process" results often in a form of "concentrate" that may be *unmarketable* in such state—being a mixture of things such as sulfides and impurities of arsenic, sulphur and the like. The marketable metal, after the "mining process", is often "captive" in the concentrate. However, there may be a market for a particular concentrate in such form, i.e., a purchaser who can use the concentrate in its business, "as is".

But the *smelter process* is different from the *mining process*. A smelter obtains or "releases" the captive or "contained" metal in a concentrate by "electrolytic depositions, roasting, thermal or electric smelting, or refining" (using the language of the 1939 Internal Revenue Code, which the parties discussed in 1941, dealing with depletion.)

The smelter treatment process makes an *unmarketable* product (a concentrate) into a *marketable metal*. Thus, an *additional value* results through the smelting process at the cost—among other things—of labor, power, supplies and reagents, and a substantial investment of capital.

A market—the source of income on which a percentage royalty is to be based—depends on whether a purchaser will buy the concentrate “as is”, for use in his business, *or* whether the “contained” or captive metal must be recovered in a marketable state *through an additional treatment process*, i.e., by treatment at a smelter.

Bradley Smelter:

There was no smelter at or near the mining property in 1941. Bradley erected its own smelter (“Yellow Pine smelter”) on the property in 1949.

Before the Bradley smelter was erected, Bradley sent concentrates to “outside” or “third party” smelters and accounted to United on the basis of a percentage of the “net smelter returns” from such smelters. There is *no* accounting question about such royalties.

After the Bradley smelter was in operation—

(a) Bradley sent $\frac{1}{2}$ of the *gold* concentrates to outside smelters, and again paid United royalties its percentage of such smelters’ net smelter returns. These payments are *not* questioned.

(b) *Bradley’s smelter treated the remaining one-half of the gold concentrates* and paid royalties to the United on the same basis as if the concentrates had been treated in outside smelters, i.e., *Bradley deducted similar smelter treatment charges—on the net smelter returns basis*. United benefited on this computation because of no deduction for

transportation to outside smelters. These smelter payments **are** disputed by United.

(c) *Bradley's smelter treated substantially all of the anti-mony concentrates* and computed royalties to United "on the basis of past practices of antimony shipments to outside smelters" with a deduction of similar smelter treatment charges, i.e., "*net smelter returns*". Again there was a benefit to United because of no deductions of transportation to outside smelters. These royalty payments **are** disputed by United.

United's Position:

United does not question the fairness of any of the Bradley smelter deductions for products of the mine treated in its smelter. *United admits that if Bradley may deduct its smelter charges*—as in the case of outside smelters—*then judgment should be for Bradley.*

But *United contends* that on the mine products which were processed at the Bradley smelter, *Bradley should not be permitted to deduct any treatment charges whatsoever*, i. e., that Bradley may not compute royalties to United under the "net smelter returns" clause.

Therefore United contends that after the Bradley smelter has reduced *unmarketable* mine concentrates to *marketable* products—Bradley should have *no* deduction for its smelting treatment charges, but should account to United by paying the percentage royalty of the price the ultimate purchaser or customer in the market pays for the finished product of the smelter i.e., under the "net revenue" provision.

United in its behalf cites no evidence whatsoever in favor of its position; relies on the face of the "plain, clear, and unambiguous contract;" and appears to be content in claim-

ing that the issue of construction was not before the trial court—a claim which will be seen to be clearly erroneous in light of this Court's opinion. (*United Mercury Mines Company v. Bradley Mining Company*, 233 F.2d 205).

Bradley's Position:

1. If given the interpretation United contends for, the "net revenue" clause makes both the "net smelter returns" and "net mint returns" clauses superfluous, *as both smelters and the mint are "purchasers"*.

2. *United's contention also completely ignores one of the "net smelter returns" provisions.* United has not even quoted this second provision. Yet the uncontradicted evidence is that at the time of the 1941 agreement *a Bradley smelter erection was contemplated by the parties.* Therefore, Bradley submits that this particular clause (R. 18) would (by the testimony) read:

"Should a [Bradley] smelter or other reduction works be erected * * * then there shall be deducted from the *net smelter* or reduction returns a fair charge for trucking * * *"

3. United has ignored uncontradicted testimony as to custom,—that the mining process is distinct from the smelting process; that the parties were searching for a market provision not involving either the smelter process or the mint; and *that the "net revenue" clause was specifically inserted as a "catch-all" to provide for a royalty from a market which was neither a smelter nor a mint—and more specifically to cover purchases in the open market of tungsten and mercury.*

4. United has ignored the uncontradicted testimony that the main purposes of the change from the 1939 agreement to the 1941 agreement was to reduce Bradley's royalties

(from a graduated $7\frac{1}{2}$, 10 and $12\frac{1}{2}$ per cent scale *to* a flat 5% scale), and to make it economically feasible to mine low grade ore.

5. United has also ignored testimony as to the *conduct* of the parties, and particularly the recognition by United for 2 years (1943-1945) of "net smelter returns" royalty computation by Bradley to United on concentrates treated at Bradley's own purification plant at Boise (*Bradley having deducted its treatment charges and depreciation, without any objection by United*).

Finally, it is agreed, that under Bradley's interpretation United has received as much *and more* in royalties than it would have received if Bradley had sent all production to an outside smelter.

Bradley, therefore, contends that—as an afterthought—United is seeking to reap windfall profits and to penalize Bradley for construction of its own smelter, by claiming that the 5% royalty should apply to the ultimate market purchase price "*of the smelter product*" i.e. 5% on the additional values added by the smelter metallurgical process—without allowance for the usual treatment charge deductions of an "outside" smelter.

The question then is, shall United get the same royalty when the concentrates go through a smelter owned by Bradley on the premises—as if they went through an independently owned smelter,—**or** *is United to get a greater royalty merely because the smelter is owned by Bradley*. The record shows a greater return to United because of the Bradley smelter operation (over that of an "outside" smelter). Rephrased, the question is whether, *in addition*, the share of the smelting costs—which would otherwise be borne by United—are to be saddled upon Bradley.

PRIOR PROCEEDINGS

This action was commenced by United against Bradley in the United States District Court in Boise, Idaho, on July 12, 1951.

(a) First District Court Proceeding.

Judge Healy sat as District Judge in the first District Court proceedings. After various proceedings the case came on for a pretrial conference. The District Court announced its construction that the "net smelter clause" was controlling. United took the position that it would only offer evidence in its case on the "net revenue" theory. On the Court's construction United conceded that it had no money claim, and consequently the complaint was dismissed. This was a summary judgment for Bradley.

(b) First Opinion on Appeal.

This Court, in its opinion of February 8, 1956, reached a different construction of the contract than did the District Court and remanded the case to the District Court for an accounting under the "net revenue" provision.

(c) Petition for Rehearing and Modification.

Thereafter on March 19, 1956, Bradley filed its "Petition of Appellee for Rehearing and Motion for Modification Under *Fountain v. Filson*, 336 U.S. 681". This Petition for Rehearing and Modification to which we respectfully direct this Court's attention, submitted that this Court's action in going beyond a mere reversal and remand was erroneous, in that it reversed a summary judgment for Bradley and directed a summary judgment for United. Bradley urged that it had been denied the right to a trial on the major

issue of the case—namely the construction of the 1941 contract.⁴

Bradley made an offer of proof as to questions raised by the text of the contract and to available extrinsic evidence pertinent to their solution (Pet. for Rehearing and Modification pp. 26-45).

(d) Order of May 15, 1956:

This Court on May 15, 1956, ordered a withdrawal of the opinion of February 8, 1956 and filed a substituted opinion.

(e) Opinion of May 15, 1956:

The substituted opinion was rendered by this Court on May 15, 1956. *United Mercury Mines Company v. Bradley*

(4) A summary of the reasons submitted for the grounds that the action of this Court in going beyond a mere reversal and remand was erroneous was given at page 3 of the petition on rehearing and modification:

(a) If the contract does not on its face clearly bear the construction given it by the District Court, then under the applicable State law (controlling under *Erie R. Co. v. Tompkins*, 304 U.S. 64), it is sufficiently ambiguous so as to permit the introduction of extrinsic evidence as an instrument of construction;

(b) Under the law of California and Idaho, upon the slightest ambiguity in a contract, extrinsic evidence is admissible in aid of its construction;

(c) When extrinsic evidence is admissible, the construction is a question of fact, the case must be tried, a summary judgment construing the document is not permissible, and the fact that one party moved for a summary judgment does not justify entry of a summary judgment against it;

(d) Particularly, in such a case, an appellate court may not construe the contract. In going beyond a mere reversal and remand for an unfettered trial, and in similarly construing the contract, the Court's decision conflicts with *Fountain v. Filson*, 336 U.S. 681.

(e) Consequently, if the judgment of the District Court is to be reversed, the case should be remanded for a trial to determine the actual intent of the parties in making the contract and to this end to receive evidence of the customs, usages and practices of the mining and metallurgical industries, the background and circumstances in which the contract was made, the contemporaneous conduct of the parties under it, and other extrinsic circumstances, some of which we shall describe.

Mining Company, 233 F.2d 205. The opinion refers to the petition for rehearing and to Bradley's contention that "there remains untried an issue of fact in that there are relevant extrinsic circumstances of which it [Bradley] is prepared to offer evidence, as bearing on the meaning of the contract." The case was remanded to the district court for a trial of the issues of fact raised by the petition for rehearing.

(f) Pre-Trial 1957:

District Judge William C. Mathes held a pre-trial conference at Boise, Idaho on February 19, 1957. As a result a pre-trial order, approved as to form and content by the parties, was issued by Judge Mathes on March 11, 1957. The pre-trial order—with certain reservations as to materiality—contains numerous admitted facts and various stipulations as to accounting, and as to common knowledge, practices and customs on the mining and smelting industries (R. 419-435). These matters will be treated later in the statement of facts and argument.

(g) Trial 1957:

On March 19, 1957, the trial commenced before Judge Mathes at Boise, Idaho (R. 75-241). After offering certain exhibits, United rested its case without presenting testimony (R. 81-91). Bradley presented testimony from an admittedly qualified expert on the facts of the case, including the circumstances surrounding the negotiation and execution of the contract, customs and practices of the mining industry, and the practical construction of the contract by the parties (R. 92-238).

United offered no rebuttal (R. 239). After oral argument, Judge Mathes commented on the evidence (R. 242-253) and held in favor of Bradley—

"The judgment will be, declaring and decreeing that the proper legal method for determining the amount of royalty due United from Bradley under the terms of the 1941 contract for the minerals, ores, metals and values extracted or produced from the mining claims described in the agreement and conveyed to Bradley and smelted at the Yellow Pine smelter, owned by Bradley, is by the use of the net smelter return provision as defined in the agreement. I am referring now to the interpretation of the prayer of the Complaint as set forth at the bottom of Page 1 and the top of Page 2 of the Pretrial Conference Order."

(h) Findings—Conclusion—Judgment.

The written Findings of Fact, Conclusions of Law and Judgment were signed by Judge Mathes and filed April 24, 1957 (R. 36-66).

STATEMENT OF FACTS

A. History—1927 to 1951.

Prior to December 31, 1941—the date of the agreement under consideration here (R. 12ff)—United owned certain mining claims in Idaho. Since 1927, Bradley and its predecessors in interest, had conducted mining operations on these claims under a succession of royalty agreements.

(1) 1939 AGREEMENT AND OPTION.

The agreement just preceding that of 1941 was entered into on May 16, 1939 (R. 339ff). It provided for a graduated royalty of 7½, 10, and 12½ per cent (10% to commence August 1, 1944, and 12½% to commence August 1, 1949, until exercise of purchase option).

Three methods were specified for computation of royalties based on "net smelter returns", "net revenue" and "net mint returns".

(2) 1941 AGREEMENT.

It is uncontradicted that the *purpose of the change from the 1939 contract to the December 31, 1941 agreement and conveyance was to reduce Bradley's royalty rate, i.e., to a flat 5%, and to make it economically feasible for Bradley to mine low grade ore* (R. 132, 133; Finding XXVI, R. 51, 52).

The 1941 agreement also contains three royalty provisions—but in more detail than the 1939 agreement—as to “net smelter returns”, “net revenue” and “net mint returns”; and also referred to as “smelter, *market*, and mint.” (R. 15-18).

For the first time, in the trial—at which uncontradicted evidence was adduced—the background was given for a proper and complete interpretation of these royalty provisions. One answer is to be found in the extrinsic evidence of the usages, customs and terminology of the mining industry at the time the 1941 contract was entered into (in addition to the later construction by conduct of the parties). This involves primarily an understanding, as known to the mining industry, of terms such as “mining,” “milling”, “concentrating”, “smelting” and other treatment processes as to materials extracted from the ground.

As the records shows, after what is known as the ordinary treatment or milling process at a mine of ores extracted therefrom, the products of such process have certain sources or *markets* resulting in “returns” on which a royalty is computed.

In the case of gold bullion, after the usual mining and treatment process, the market would be the U. S. Mint. The return from the mint is known as “*net mint returns*”.

Other products of the mining and milling process—such as antimony—*would necessarily have to go to a smelter in the form of concentrates for additional treatment and refin-*

ing before a marketable end product is obtained. The return to the mine operator from the smelter, reflecting the smelter's treatment charges, is known as "*net smelter returns*".

However, certain minerals after being mined and concentrated are then in a product form for use by certain industries. *These concentrates, the end product of the mill or concentrator, are marketable without the added treatment of the smelting process.* Such a type of concentrate coming from the mill or concentrator is then ready for "*market*". The record, we submit, supports our contention that the "*net revenue*" provision was designed solely for the purpose of providing a royalty upon such a directly marketable product.

The three royalty provisions in the 1941 agreement reflected the different *markets or sources of income* from the past operational experience as to the mine's output. They also reflected well known customs and practices of the mining and smelting industries at the time (Finding XXXIV, R. 55).

In this latter connection, it was *stipulated* (R. 427)—

"That it is a matter of common knowledge and historically recognized in the mining industry that *the milling of ores to reduce such ores to a concentrate form is a part of the mining process and that the smelting of ores is not a part of the mining process.*"

It is historically recognized in the mining industry that *the smelting process adds value to the products of a mine* (R. 191).

Before the execution of the 1941 agreement the parties knew that the mining property contained ores and values such as *gold, silver, antimony, tungsten and mercury* (i.e., quicksilver and sometimes described as cinnabar).

"Net Smelter Returns"

Prior to the 1941 agreement, concentrates from *antimony-gold* ores mined and milled (or concentrated) on the property were shipped to "outside" or "third party smelters" (not owned by Bradley). The smelters' settlements or "net smelter returns" reflected, among other things, the customary deduction for the smelter's treatment charges. Bradley's royalty payments to United were based on a percentage of these "net smelter returns".

Accordingly, the 1941 agreement contained the provision —(R. 17),

"By *net smelter returns*, as used herein, is meant the amount received from the smelter * * * *it being understood that the smelter will deduct its normal smelting charges* * * *"

Here it should be noted that *the 1941 agreement also provides* (R. 18):

"*Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.*"

What smelter erection was in the contemplation of the parties in 1941? The uncontradicted testimony in this record is that the parties had discussed the possibility of a smelter being erected at or near the mining property. *The parties contemplated that such a smelter would be erected by Bradley* (R. 131, 134; 160-164; Finding XXVIII R. 52, 53).

See also the earlier provision of 1939 agreement (R. 352) "** * * Should local reduction of the concentrates become practicable as determined by the Optionee* * * *". The Optionee, of course, was *Bradley*.

The foregoing will be considered in detail in a later discussion of United's sole contention in this case—that the *Bradley* smelter, later erected in 1949, should *not* be permitted “to deduct its normal smelting charges.”

"Net Mint Returns".

Referring now to the remaining two sources of royalty income (other than a smelter)—in the early 1930's *gold* bullion had been produced at the mine and shipped to the U. S. Mint (R. 108, 109). Hence reference in the agreement to “*net mint returns*”. This clause is not involved in this action.

"Net Revenue".

The parties in December 1941 knew that there was *another source of income for royalty computations that was neither a smelter nor a mint. In the middle of 1941 tungsten was discovered at the property.* (R. 134, 135) :

“Q. After the 1939 contract was signed, and before the 1941 contract was signed, *was there any discovery on this property covered by this litigation, of any product which could be mined and which could be mined and which would not or could not be sold to a smelter?*”

A. Yes, sir.

Q. What product was discovered on the property?

A. *Tungsten.*”

Commencing in August or September of 1941, tungsten concentrates had been shipped *directly to a market—i.e., purchasers or customers—who used the concentrate product without involving the smelting process.*

Royalty was applied and paid by Bradley to United in the Fall of 1941 on the “net revenue” from such purchasers (R. 136-143).

At the time the 1941 agreement was executed there was no custom in the history of tungsten mining to send tungsten ore to a smelter (R. 143).

In addition to tungsten, the parties were aware of *mercury* on the property—a potential mine product that needed no treatment by a smelter and could be sold directly to purchasers (R. 109, 135, 136).

For the first time in this case there is specific testimony—which is uncontradicted—as to the reason for the inclusion of the “net revenue” clause, i.e., “the discovery of tungsten and the knowledge of mercury in the district,” (R. 134, 135, 194); and **“the reason being that we had other mineral products that were not covered by the net mint and net smelter clauses”** (R. 230).

The “net revenue” clause is aptly described by Judge Mathes as a “*catch-all*” provision to cover a recognized market which was neither smelter nor mint (R. 249).

And see the testimony at R. 186:

“We were hunting for a clause that would cover products that would not go to a mint, such as gold bullion, or sulfide concentrates that would go to a smelter.”

(3) OPERATIONS AFTER DECEMBER 31, 1941.

During this period to 1949, Bradley continued to ship antimony-gold concentrates to smelters and accounted to United on the “net smelter returns” basis.

But the most important part of the mining operation in the history of the mine from beginning to end, dollar-wise and tonnage-wise, was the continued production of tungsten—after the discovery and substantial shipments prior to December 31, 1941 (R. 183, 184). From 1941 into the year 1945 *Bradley shipped tungsten concentrates from the mine direct to purchasers, other than smelters*, and paid royalties to United based on the “*net revenue*” provision (R. 142; Findings XXIX, XXX, R. 53, 54).

(4) BRADLEY'S BOISE PURIFICATION PLANT OPERATION FROM 1943 INTO 1945—CONSTRUCTION OF CONTRACT BY CONDUCT OF PARTIES.

In 1943 *Bradley constructed its own plant* at Boise, Idaho—known as the Boise Purification Plant. The purpose of the plant was to treat and further purify some of the tungsten concentrates extracted from the property—by removal of phosphorous, antimony, sulphur, arsenic and other impurities—before shipment to the market.

Bradley operated its Boise Purification Plant for approximately two and one-half years.

The Boise Plant treatment process was according to mining industry practices and custom “outside the realm of mining” (R. 142, 145).

During all of that period—1943 into 1945—Bradley computed and paid royalties to United on the proceeds of all sales of tungsten concentrates processed and treated at its Boise Plant, after deducting—from the proceeds of such sales—the operating costs and depreciation of the Boise Plant.

Monthly settlement sheets were submitted by Bradley to United with complete information as to all sales and deductions made by Bradley for operating costs and depreciation (R. 146-150).

The method of settlement by Bradley with United, as to computation and payment of royalties, was under the “net smelter returns” provisions of the 1941 agreement (R. 148; Findings XXXVII and XXXVIII, R. 57, 58).

All payments were accepted by United without any protest or objection (R. 149):

“Q. Now did anyone representing the Plaintiff, United Mercury, ever complain or object to the method of settlement?

A. No.”

It should be mentioned that *this testimony as to the conduct and construction of the contract by the parties commencing two years after the execution of the 1941 agreement—and extending for two and one-half years into 1945—was uncontradicted* and was introduced without objection as to admissibility.

(5) BRADLEY SMELTER—1949.

After the cessation of tungsten production, Bradley decided in 1948 to erect a smelter at or near the property. It was principally designed for the production of antimony.

In 1949, Bradley's smelter, known as the Yellow Pine Smelter, was erected at the property at a cost of approximately \$2,000,000.00. The cost of maintaining the operation was borne exclusively by Bradley (R. 167, 168, 182, 183; Finding VII, R. 42). *As has been mentioned, the contracting parties in 1941 foresaw this eventuality by including a specific provision in the 1941 agreement contemplating a local smelter construction* (R. 18),—a Bradley smelter (R. 131, 134; 160-164).

Thereafter substantially all of the antimony concentrates went into the Yellow Pine smelter. However, one-half of the gold concentrates went to "outside" or independent smelters. It was impossible to ship all of the gold concentrates to outside smelters owing to high arsenic and antimony content—and certain smelters refused to accept such a heavy tonnage of gold concentrates (R. 169, 170).

The *royalties* paid by Bradley to United on account of gold concentrates treated in the Yellow Pine smelter were computed on exactly the same basis as the net smelter returns from outside smelters, except that United benefited substantially because of non-deduction of freight (R. 171). Thus, United received more in royalties than if Bradley had sent all of the mine production to an outside smelter.

The uncontradicted testimony is that the *royalty computed on the antimony concentrates treated and processed at the Yellow Pine smelter was "on the basis of past practices of antimony shipments to outside smelters"* (R. 171):

"Q. How did you compute the royalties paid on account of the gold concentrates treated in the Yellow Pine smelter?

A. On exactly the same basis as the net receipts from the American Smelting and Refining Company, except in the beginning we did not deduct any freight so that the United Mercury Mines benefited substantially.

Q. How did you compute the royalties on the antimony concentrates treated in the Yellow Pine smelter?

A. On the basis of past practices of antimony shipments.

Q. To outside smelters?

A. To outside smelters."

And see R. 173:

"Q. Did you report to the Plaintiff your computation on account of antimony concentrates that were treated in your own smelter?

A. Yes, we reported to the Plaintiff.

Q. That was beginning then in August of 1949, and continuing until 1952?

A. Yes.

Q. Did the defendant compute and pay royalties in accordance with that method on all the concentrates, the antimony concentrates that were ever treated by the Yellow Pine Smelter?

A. Yes."

(6) 1950 SUPPLEMENTAL AGREEMENT.

There was a supplemental agreement negotiated between the parties on July 20, 1950 (R. 377-381). That contract is referred to in the testimony (R. 173-177).

It is to be noted that (R. 175, 378) one of the "whereas" clauses recites in part:

"The said *Bradley Mining Co. did*, on the 20th day of June, 1950, *pay* to the United Mercury Mines Company *the royalties due for the month of May, 1950.*"

In the agreement itself there is the following provision (R. 175, 380):

"*It is further agreed* that said *Bradley Mining Co. shall make the usual monthly reports* as to moneys received by it during the preceding month upon which royalties would be payable, stating the amounts of royalties that had accrued, but, instead of sending the check as has been the practice during the past ten years, shall make a notation thereon to the effect that the above accrued royalty has been postponed * * *"

The evidence is uncontradicted that royalties paid to United upon the products of the mine treated by Bradley at the Yellow Pine smelter before, in and after the month of May, 1950 were computed and paid according to the "net smelter returns" method provided for in the contract of December 31, 1941.

(7) PAYMENT OF ROYALTIES ON NET SMELTER RETURNS METHOD MADE FOR APPROXIMATELY TWO YEARS WITHOUT OBJECTION.

The uncontradicted evidence is that no one representing United objected to the method in which Bradley had been computing royalties on materials that went through the Yellow Pine smelter, i.e., on the *net smelter returns* basis—for approximately two years after the Yellow Pine smelter was placed in operation. The first objection was made in about mid-1951 (R. 178, 179).

And see Finding XLI (R. 61):

"That the defendant has computed and paid royalties to the plaintiff upon products of the mine treated and

processed by the defendant at the Yellow Pine Smelter on the same basis and utilizing the same treatment schedule, but without deducting freight charges, as in the case of identical concentrates shipped to outside smelters; the net effect being that plaintiff benefited in royalty payments when identical concentrates were smelted by the defendant at the Yellow Pine Smelter as compared with the best arrangement that could be made with an independently owned smelter; and the plaintiff did not object to the payment of such royalties by the defendant upon the basis of 'net smelter returns' until 1951."

(8) UNITED FILES ACTION AGAINST BRADLEY—JULY 1951.

This is the end of what we have called the "history" of the operation at the mining property.

United's contention is that—although third party smelters' deductions for treatment charges are proper—Bradley cannot deduct its "normal smelting charges". No other question is raised. United concedes that if Bradley is allowed to account to it under the "net smelter returns" clause on mine products processed in the Bradley smelter, then the judgment shall be affirmed. In short, **it was admitted at the trial that if Bradley is permitted to deduct its smelter charges—as in the case of other smelters, "judgment is for the defendant" (Bradley) (R. 239, 240, 241).**

In the long history of operations from 1927 to 1951 there is no other accounting contention—*the issue is only as to concentrates processed by Bradley in its own smelter from 1949. United does not claim the Bradley smelter treatment charges are unfair or excessive.* Its sole contention since the action commenced is that the "*net revenue*" clause governs; that United's royalty percentage should apply on a purchaser's or customer's payments for the *product of the smelter*—i.e., *on the value added by the smelter process*, with no al-

lowance whatever for the historically recognized deduction by a smelter for its treatment charges.

From the commencement of the action, United has refused to come to grips with the facts, circumstances, customs of the industry, or practical construction of the contract by the parties. United's Opening Brief is typical. The District Court's Findings, according to United, are "immaterial". (App. Op. Br. p. 10). Apparently, to United, the pre-trial and trial before Judge Mathes at Boise were a waste of time because, as United contends, the disputed portions of the 1941 agreement are "clear, plain and unambiguous" in United's favor (App. Op. Br. p. 11).

Both sides initially took the position that the contract was unambiguous and clear on its face. But, although United is still unwilling to accept the situation in its Opening Brief, it is now apparent that language in the contract of December 31, 1941, is susceptible of more than one interpretation and is ambiguous. There is not only the dispute of the parties, but also the fact that Judge Healy, sitting as the District Judge, gave one construction, this Court gave a different construction, withdrew its opinion, rendered a substituted opinion, and remanded the case for a further hearing upon the merits in the District Court.

Judge Mathes makes the following comment (R. 242) :

"The Court: The contract is admitted and the salient features that we are involved with are, of course, as set forth on pages 15 to 18 of the record on appeal, which is excerpted from Exhibit Seven here.

We bear in mind that the contract was made in 1941 and the smelter built in 1949. Our problem here is to ascertain the intention of the parties in the light of the facts and circumstances in evidence surrounding execution. The controversy arises, of course, because *the contract is unclear as applies to this subsequently constructed smelter operation on the property, although*

admittedly the contract contemplated the possibility. It did not literally in so many words cover the contingency of the smelter on the property owned and operated by one of the parties to the contract."

In the foregoing chronology, brief references have been made to some of the "facts and circumstances in evidence surrounding execution" of the 1941 agreement. To give a more complete presentation, we will set forth additional extrinsic evidence. We also feel it helpful to elaborate upon some of the points already touched upon.

B. Discussion of Extrinsic Evidence.

In the Petition for Rehearing and Modification (pp. 26-45) above referred to, an "offer of proof" was made, of available extrinsic evidence pertinent to the solution of the questions raised by the text of the 1941 agreement. We submit that the uncontradicted testimony, and the pre-trial stipulations fully support *and go beyond* the offer that was made.

(1) SMELTER AT PROPERTY CONTEMPLATED BY PARTIES IN 1941 WAS A BRADLEY OWNED SMELTER.

Referring to the above comment of Judge Mathes as to the "contingency of the smelter on the property owned and operated by one of the parties to the contract," the record is clear *and uncontradicted* that as early as 1939 *the parties discussed and contemplated a possible smelter erection by Bradley and only by Bradley* (R. 131-134; 160-165).

Research as to the best methods of local reduction (i.e. smelting) "starting in the early thirties" was made by Bradley and Bradley would report to United "periodically as to our progress." (R. 133, 134).

And see (R. 162, 163)

“Q. When did you talk to the people on the other side about the possibility of smelting or local reduction? * * *

A. At numerous times.

The Court: Commencing when?

A. Commencing in late '38 through '40, I will say late thirties and through the forties * * *

The Court: Did you ever talk with Mr. Oberbillig [President of United] about the possibility of a smelter being constructed at the mine?

A. Yes * * *

The Court: About when?

A. The late thirties * * *

The Court: At the time you were negotiating the contract, —in 1941 were there any negotiations about it.

A. Yes.”

The record, as to *who* might build the smelter under discussion, definitely shows the contemplation of a Bradley smelter (R. 164):

“The Court: I asked was it discussed, about the possibility of one being built?

A. Yes.

The Court: The maybe's of the situation were discussed?

A. Yes.

The Court: *And that referred to the possibility that the defendant here might build?*

A. Yes.”

As the record shows, a smelter is also referred to as a refinery plant or reduction works.

It is to be noted here that in the 1939 agreement between the parties the possibility of an erection of a smelter by Bradley was *specifically* referred to. (See agreement of May 16, 1939, R. 339 at R. 352):

"It is understood, however, that should local reduction of the concentrates become practicable *as determined by the Optionee*, that no concentrates will be shipped."

Bradley, as mentioned before, was the "Optionee".

And now let us refer to a similar or expanded paragraph in the December 31, 1941, contract (R. 12 at R. 18). The uncontradicted testimony refers to this paragraph, and is as follows (R. 164) :

"Q. Will you observe, Mr. Bradley, there in the first paragraph beginning on that page, '*Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.*' Now, was that provision discussed among you before this contract was signed?

A. Was it discussed before the contract was signed?

Q. Yes?

A. Yes.

Q. When I say discussed, I mean with the other side?

A. Yes.

Q. Was there any suggestion made that should reduction works be erected they would be erected by anyone except Bradley?

A. No."

The emphasis in the above quoted paragraph with regard to trucking charges, in the light of the above testimony, points up the fact that should a *Bradley smelter* be erected, the Bradley smelter should be able to "deduct from the net smelter or reduction returns" a fair charge for trucking.

With this key word inserted the provision reads "should a **Bradley** smelter or other reduction works be erected * * *

then there shall be deducted from the net smelter or reduction returns a fair charge for trucking."

There was no cross examination on the above quoted testimony—and no rebuttal.

A glance at United's opening brief will suffice to show that this testimony is not discussed. Nor is the above quoted smelter return provision even included in the royalty clauses that United has quoted as being applicable to this case.

Here also it must be pointed out that it has been stipulated by the parties in the pre-trial order that if Bradley is entitled to make any charge or deduction for smelting at its Yellow Pine smelter for all ores processed through it, then all royalties have been paid and there is nothing more due or owing to United. (See pre-trial order R. 425, 426).

"That, if under the terms of the contract, defendant, Bradley Mining Company is entitled to make any charge or deduction for smelting ores in the Yellow Pine Smelter, the charges and deductions so made by Bradley Mining Company have been proper charges and deductions and all settlements made with the plaintiff have been correct.

"If it is ultimately determined that the net smelter returns provisions of the agreement is applicable to the operations at the Yellow Pine Smelter for ores, concentrates, metals and values taken from the claims described in the agreement, then the settlements made by Bradley have been correct as to the minerals, ores, metals and values processed at the smelter."

And see the admissions of counsel for United (R. 240):

"In other words if the net smelter returns provision applies the judgment is for the defendant * * *";

And at R. 241:

"If the net smelter returns provision applies we are still not interested in an accounting, because it is

admitted that they have properly accounted for everything under their theory of the net smelter returns."

(2) CUSTOM—INTRA COMPANY ACCOUNTING—"NET SMELTER RETURNS RECEIVED."

There is another matter of custom which is stipulated to in the record. This bears upon the language "net smelter returns" and "amount received from the smelter." There has been some contention that this word "received" connotes payment by a third party or "outside smelter" and that therefore the "net smelter returns" clause may not be applicable to a smelter owned by Bradley.

Actually in the industry this term signifies net realization after smelting, whether by way of cash paid or credit given. This is caused by the fact that in many instances a mining company owning and operating a smelter will also own and operate mines, and settle on the same basis as such smelting or mining companies would settle with independent customers. This was the practice and custom of the trade where ores treated came from mines owned by the owners of smelters or came from mines leased and mined by the smelter owner, or came from independent custom shippers. The resultant accounting or settlement is a reflection of the smelter charge and cost of transportation if any. The net amount was commonly referred to in the mining and smelting industries as "net smelter returns".

Because of the importance of this stipulation which shows that this custom was in effect before the 1939 and 1941 agreements we are setting it out in full (R. 426, 427):

S. That before 1939 and thereafter at all times material to this action it was the practice and custom in the smelting industry for companies who own and operate smelters to also own and operate mines; that it was likewise the practice and custom in the industry for companies owning mines and also owning smelters to

ship their mine products to their own smelters; that it was likewise the practice and custom with respect to owners of smelters and mines to also lease mining properties from other independent owners and send the products extracted therefrom to their own smelters and to settle for the products so shipped on the same basis as such smelting companies would settle with independent or custom shippers; that it was a practice and custom of the trade that where ores treated came from the mines owned by the owners of smelters, or came from mines leased and mined by the smelter owner, or came from independent custom shippers, that the smelting charges and the cost of transportation of concentrates to the smelter were deducted to arrive at a net amount commonly referred to in the mining and smelting industries as "net smelter returns". (Stipulation).

Similarly the uncontradicted testimony is to the effect that the foregoing custom was in effect in Idaho in 1939, and that it was the custom and practice "for separate records to be kept as to the production of the mine as distinguished from the production of the smelter" where a mining company smelted ores from properties 100% owned, 50% owned and on a lease and option basis" (R. 129, 130).

(3) PURPOSE OF CHANGE FROM 1939 TO 1941 CONTRACT.

It is uncontradicted that one of the purposes of the 1941 agreement was to reduce the amount of royalty required to be paid by the appellee. The 1939 contract provided for a graduated royalty: 7½% from 1939 to 1944; 10% from 1944 to 1949 and 12½% from 1949 and thereafter (R. 351, 352).

See the uncontradicted testimony at R. 132-133:

"Q. You stated that negotiations for the 1941 contract began sometime early in the year and that you

discussed the matter with the representatives of the plaintiff, and I asked you then if you stated the reasons why you wanted the contract changed, and you said 'Yes,' now, what were those reasons?

A. The reasons were that the '39 contract, in our minds, was going to become burdensome owing to the royalty, the graduated royalty schedule contained in it.

Q. The royalties were too high?

A. The royalties were higher than we thought we could economically bear. In other words, ore that would be ore under a certain royalty would not be at the higher rate of royalty.

Q. Would that then, in effect, place a limitation on the mine?

A. Yes, sir, oh yes.

Q. Now, coming to another subject, Mr. Bradley—
The Court:—Was this told to the Plaintiffs?

A. Yes, as the reason, our reason for wishing it.

The Court: I will reverse the ruling on that, I think that should stand,—that answer, as the reason why the contract, why the 1939 contract was terminated and the new contract was negotiated. It being a motive or purpose expressed to the other party, that, in my opinion, would be admissible."

The significance of the change from the 1939 contract to the 1941 contract is aptly commented upon by Judge Mathes (R. 251).

"One of the most compelling purposes or one of the most compelling considerations, as I find it in interpreting this contract, is the purpose the parties had in setting or putting aside this 1939 agreement, and creating the 1941 agreement. It is admitted that the purpose of the defendant, of course, was to get the lower royalties, but important here is the purpose of the plaintiff in granting the lower royalties, and that purpose was to induce and make it economically feasible and attractive for the defendant to mine ores of a lower quality.

It's admitted here that the construction of this contract, which would not permit the defendant to deduct the smelting charges, would result in substantial increase in the amount of the royalty over that that would be payable were the net smelter returns provision to apply whenever ore is smelted. That in itself as I view it and find, would be a construction contrary to the purpose of the contract and contrary to the plaintiff's own avowed purpose at the time the contract was executed."

(4) SMELTING IS NOT CONSIDERED PART OF A MINER'S ORDINARY TREATMENT PROCESSES.

Mining is—in part—the extraction of various minerals or ores from the ground. But mining, as known in the mining industry, is also the treatment or "dressing" of ores in a plant, mill or concentrator. Such treatment is part of a *mining process*. The *smelting* of ores is *not a part of the mining process*.

See again the pre-trial stipulation (R. 427):

"T. That it is a matter of common knowledge and historically recognized in the mining industry that the milling of ores to reduce such ores to a concentrate form is a part of the mining process and that the smelting of ores is not a part of the mining process. (Stipulation)."

And see the testimony at R. 204:

"The product from the mine stops when the production process is complete so far as mining concentration terminology is concerned. It does not involve steps such as smelting that completely change the character and reduce the mined product to a metal."

A mine of any consequence has a local treatment plant for its ores—usually a mill or concentrator—depending upon what is being mined. Although it is customary throughout the mining industry for mines to be equipped with some

sort of treatment or concentration facilities, the number of mines outnumber the number of smelters in the industry by a wide margin. It is not economical in the mining industry for the ordinary mine to be equipped with a smelter (R. 180).

The treatment in the mining process varies. For example, a **gold** mine may have—as this property did prior to the 1939 and 1941 agreements—a concentrator in the form of a cyanide plant. This treatment resulted in gold bullion. The market for this bullion—and the only market for years—has been the United States Mint. (R. 108, 109). The mint—or market—meant “net mint returns” to the mine operator. There is no dispute as to the meaning “net mint return” clause of the contract (Pre-Trial Order stipulation “R,” R. 426).

As to **mercury**, (quicksilver or cinnabar) which the parties were aware existed on this mining property, the custom and the practice in the industry at the time the contract was formed for concentrating the product was a treatment process of roasting, condensing the fumes and recovering the marketable product at the mine. This is regarded as part of the mining process (R. 135, 136). The market for mercury as a *metal* and end product of the concentrating process was *not* a smelter—the finished product being sold directly on the market for use by consumers (R. 109-135, 136).

As to **tungsten**, the custom and practice of the mining industry, at the time of the contract, was to treat the ore in a concentrating plant at the mining property by a combination method of flotation and gravity—referred to as either milling or concentrating of ores, and resulting in an end product called tungsten concentrates. This concentrating method was recognized in the industry as a part of the mining process.

Bradley began making tungsten concentrates in 1941 and commenced shipment in either late August or late September, 1941 (R. 136-138). The tungsten concentrates were marketed for direct use in such form by consumers (R. 139-142). There was no custom in the history of tungsten mining at the time of sending tungsten ore or tungsten concentrates to a *smelter* (R. 143).

As to the production of tungsten concentrates— it should be stressed that these concentrates shipped by Bradley to customers and consumers direct on which the “net revenue” clause would apply because no smelter process was involved, became the most important part of the mining operation in the history of the mine from the beginning to the end, tonnage-wise as well as dollar-wise (R. 183, 184; Finding XXIX, R. 53).

As to **antimony**—prior to 1937 ores extracted at the property were processed into concentrates having a combination of antimony and gold. (R. 103). In accordance with the practice of the industry in the disposition of antimony and gold concentrates, and prior to the 1941 contract, these concentrates were sold to a smelter which was the *market* resulting in “net smelter returns,” (R. 109) reflecting treatment and other charges.

Here the mining process involved extraction and treatment at the mining property to produce concentrates. In order to obtain a finished product it was necessary that additional treatment, i.e., *smelting*, be done which completely changes the character and reduces the mined product to a metal (R. 204). *In other words the end product or finished product was not obtained until it had gone through the smelter treatment process* (R. 214).

(5) THE SMELTING PROCESS—ADDED VALUE:

It has been admitted that the smelting of ores is not a part of the mining process. In the mining industry at the time of the 1941 contracts, the term "smelting" had and always has had a special signification (R. 144). The three essential steps of smelting are roasting, reduction and refining (R. 127, 144). Because of the capital outlay and economics involved, smelters are rare and the usual custom is for a mine not to have a smelter. (R. 212). In the history and practice of the trade it is well known that *smelting* adds value to the products of a mine. The uncontradicted testimony is as follows: (R. 191).

"Q. Mr. Bradley, does the smelting process add value to the products of the mine?

A. Yes.

Q. Will you explain that briefly?

A. You are taking, in effect, a crude material that is very close to its native state, still containing gangue materials, impurities such as arsenic, sulphur and so forth. The product from the mine, being the product from the mine and the concentrator not having any use, whereas the end product after smelting and refining having a use, it being reduced down to its final state for manufacturing purposes. *An example in case of antimony is the history and practice of the trade has been that the ore or concentrates is approximately one-half of the value of the finished product.*"

(6) 1939 INTERNAL REVENUE CODE:

As one of the surrounding circumstances, the uncontradicted testimony shows that *at the time the 1941 agreement was being formed tax problems involving depletion were discussed by the parties* (R. 210). This Court may take judicial notice, as the District Court did, of the fact that Section 114(b) (4) (B) of the Internal Revenue Code

of 1939 defines "gross income from the property" as meaning the "gross income from mining".

The definition of the term "mining" as contained in that section of the U. S. Internal Revenue Code includes the ordinary treatment processes which, as we have shown, according to the universal usage and custom in the mining industry, are considered to be a part of mining. But it excludes from the definition of "mining" the additional process for purification and treatment of ores and minerals such as "roasting, thermal or electric smelting, or refining" (Finding XXIII, R. 47).

It is obvious from the uncontradicted testimony as to the practices, usage and custom in the mining industry at the time the 1939 and 1941 contracts were executed that there was a definite statutory recognition of the industry distinction between *mining*, and the *smelting* or metallurgical process (R. 193). In other words, depletion allowance, as recognized in the Internal Revenue Code, was permitted as to income from the *ordinary mining process*, but was *not permitted in connection with income from products to which value had been added by the smelting process*.

It should be noted here that, as mentioned above, tungsten was discovered, and a substantial amount of tungsten concentrates were produced at the mine, before the 1941 contract. The treatment process was "a combination of flotation and gravity concentration method * * * at the property" (R. 137). This is one of the processes that was included in the above Internal Revenue Code section among "the **ordinary** treatment processes" applied by mine owners or operators (see Judge Mathes' comments R. 246-248).

(7) THE "NET SMELTER RETURNS" CLAUSE

Extrinsic evidence throws light on the meaning and scope of this provision. It reads (R. 17) :

"By *net smelter returns*, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, *it being understood that the smelter will deduct its normal smelting charges* and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted."

(a) The Word "Normal".

The net smelter returns clause provides in part,

"it being understood that the smelter will deduct its *normal* smelting charges * * *"

The record shows that the word "normal" as to smelter charges was first introduced into the 1939 contract (R. 352-353). The testimony is that the word "normal" is in the handwriting of the witness who had represented the appellee in connection with the formation of both the 1939 and 1941 contracts (R. 233; see Def's Ex. 5a, R. 372-376).

It is uncontradicted that the word "normal" in connection with smelter charges and deductions is not and was not commonly used or customarily used in connection with the sale of concentrates to "outside smelters" or independent smelters (R. 160):

"Q. Is the word 'normal' customarily used in connection with the sale of concentrates to outside smelters?

A. No."

This portion of the 1939 contract was carried into the net smelter return clause in the 1941 contract (R. 17). *It is clearly apparent from the record that this insertion of "normal" as to smelting charges was made in connection with the contemplation of the parties that a smelter might be erected by Bradley* (R. 123, 124). In brief, the word "normal" was inserted as a "protective device so that we could not overcharge Oberbillig. * * * in the instance * * *

ing, for example, would perhaps not cover the actual mercury processing. You might have high grade ore that wouldn't be milled."

(c) "**Produced from Said Properties**".

Referring to the "*net revenue*" clause of the 1941 contract which contains the words "*produced from said properties*", the uncontradicted testimony is that *in the mining industry these words have a special usage and meaning*. They mean materials produced by the mining process which includes extraction and the "*ordinary treatment process*" at the mining property (R. 199-204) at R. 204:

"The product from the mine stops when the production process is complete so far as mining concentration terminology is concerned. It does not involve steps such as smelting that completely change the character and reduce the mined product to a metal."

In other words, the *product of a smelter is not*, in mining industry usage, "*a product of the properties*".

For the first time, testimony—which was uncontradicted—clearly showed the customs and usage underlying the three royalty provisions, the surrounding circumstances, and the meaning and intent of the parties as to the "*net revenue*" provision applying to markets or customers (neither mint nor smelter) where no smelting treatment is involved.

See Judge Mathes' comment (R. 249):

"The emphasis upon market is persuasive in the light of all of the other circumstances, that the parties have in mind here possible marketing methods, envisioning the possibility over the years, so they, as to anything marketable, in a condition to be marketed, the mint,—at the time they contracted the mint was the market. As to anything required to go to the smelter, the smelter was the market. **As to other matters, as to concentrates,**

ores, metals or values, the net revenue provision was intended as a catch-all,—another method of marketing direct from the property. In other words, by transporting the product directly from the mine to the mint whenever the quality would permit such a relatively simple operation; by sending it to the smelter to be processed in the customary way, and in the third place, by marketing ore concentrates and values direct to third persons from the mine, after the mining process had been completed. This evidence of custom and practice and other surrounding circumstances and subsequent conduct is not contradicted.”

(9) PRACTICAL CONSTRUCTION—CONDUCT OF PARTIES.

We have already referred to the conduct of the parties as to the construction of the 1941 contract. Such matters as the acceptance by United of the “net smelter returns” method of computation for two years in connection with Bradley’s Purification Plant at Boise, and the 1950 supplemental agreement, will also be discussed in the argument that follows.

Argument

I.

ANALYSIS OF UNITED'S POSITION

Appellant has made no effort or attempt to demonstrate in its opening brief on this appeal the basis for its specifications of error other than to say (a) that the District Court’s findings and conclusions “are irrelevant and immaterial in view of this Court’s decision of May 15, 1956”; (b) that the disputed portions of the contract are “clear, plain and unambiguous” making extrinsic evidence unnecessary; (c) that “all of the matters adduced by Bradley at the trial were mentioned, covered and dealt with in the contract itself”; and (d) that “Bradley at the trial of this

cause presented no matters which were not before this Court at the time of its opinion of May 15, 1956" (Appellant's Opening Brief, pp. 9-14).

These laconic statements are made by appellant despite the pre-trial, the pre-trial stipulations included in the pre-trial order, the findings of the District Court that the contract was *unclear* (R. 242) and the uncontradicted testimony above referred to in our Statement of Facts.⁵

Furthermore, as has been pointed out earlier, the ambiguity of the 1941 contract is quite apparent where the various judges of this Court and the District Court have differed—demonstrating that the contract is susceptible of different meanings, is ambiguous and evidence of extrinsic circumstances is therefore admissible.

At least *there is no question that the case was remanded to the District Court for trial with specific reference to the extrinsic evidence—offered as a matter of proof—by Bradley's petition for rehearing.*

Other than the citation of one case which is not in point and the above referred to contentions that the evidence and findings were immaterial, there is no specific presentation by United as to the admissibility or inadmissibility of the extrinsic evidence which was admitted at the trial.

Apparently appellant is relying solely in its appeal on two statements in the opinion written by Judge Denman (233 F.2d 205, 207).

The first refers to the "net smelter returns" clause and the statement in the opinion is "by its terms this clause is limited to situations where 'amounts are received [by Bradley] from [outside] smelters'".

But as is shown by this record there is no basis whatever for the above bracketed insertions of "Bradley" and "out-

(5) Whether Appellant has properly complied in its opening brief with this Court's Rule 18, Sec. 2(d) will be discussed later.

side". In the first place the pre-trial order in this case contains a *stipulation* of the parties as to the custom in effect at the time the contract was executed, as to intra-company accounting and settlements by companies and *by companies that owned both a mine and a smelter*, in connection with the furnishing of what are known as "net smelter returns" (R. 426-III-"S").

Secondly, the uncontradicted testimony is that erection of a smelter by *Bradley*—not by anyone else—was contemplated by the parties and it is to be noted that neither the appellant in its opening brief nor this Court's opinion of May 15, 1956, in its recital of the contract provisions, made any reference whatever to the pivotal clause in the contract (R. 18) clause "*should a smelter or other reduction works be erected * * ** then there should be deducted from the *net smelter or reduction returns* a fair charge for trucking * * *". But as shown earlier by the uncontradicted testimony, the key word "*Bradley*" must be inserted in this clause which definitely would permit Bradley to make an accounting to United under the "net smelter returns" clause if it erected a smelter. And this was borne out by the subsequent conduct of the parties i.e. the "net smelter returns" method used by Bradley, and accepted by United without objection, at Bradley's Purification Plant at Boise, Idaho.

United's main contention is that this Court, in its opinion of May 15, 1956, ruled out any applicability of the "net smelter returns" clause to the operations of the Yellow Pine Smelter (App. Br. p. 13). The comment of this Court relied on by United is "we see no reason why, as a matter of law, the 'net revenue' clause *could* not be controlling". United's position is clearly erroneous, because United fails to consider the additional portions of this Court's opinion which supply the reason for remanding the case. This Court said:

"We see no reason why, as a matter of law, the 'net revenue' clause *could* not be controlling. The District

Court erred in granting summary judgment for Bradley. In its petition for a rehearing, following an earlier opinion for which this one has been substituted, Bradley urges that notwithstanding the views here expressed, as to the 'net revenue' clause, there remains untried an issue of fact in that there are relevant extrinsic circumstances of which it is prepared to offer evidence, as bearing on the meaning of the contract.

"Whether such extrinsic evidence is or would be admissible, or whether the writing, as drawn, so precisely fits the very circumstances here, involving amounts paid by purchasers from the sale of metals, that it must be said that all negotiations were "integrated" in the written instrument, must await decision following further hearing in the court below. (Citing Wigmore on Evidence, (3rd Ed.) Sec. 2430)."

But this Court obviously did not make a holding that the "net revenue" clause *is* controlling. Such a determination

(6) With reference to the comment on "integration" and to Wigmore, this is one of the familiar rules on admissibility of extrinsic evidence. The Court points out that extrinsic evidence is admissible on this question of integration. In addition there is the question of *interpretation*. This function of interpretation must be performed as indicated in the authorities cited herein. Even an "integrated" agreement is to be interpreted in the light of "all operative usages and all the circumstances prior to and contemporaneous with the making of the integration." See Restatement of Contracts, Section 230. And see the reference to 9 Wigmore on Evidence, 3rd Ed., 5, in this Court's decision in *Quon v. Niagara Fire Ins. Co. of New York*, 190 F.2d 256 (9 Cir.) where it was aptly said:

"The writing under these circumstances must be viewed in its setting together with all the other evidence in light of the credibility accorded the witness. Here the writing is one of the collateral facts. * * *

"Under such circumstances, the use of the cliché that the appellate court is in as good a position as the trial judge to construe a writing is futile."

See also the following portions of this brief for authorities that "upon the slightest ambiguity in the contract, extrinsic evidence is admissible in aid of construction."

would, we submit, be in effect the holding in its prior opinion of February 8, 1956, which was withdrawn after the filing of appellee's Petition for Rehearing and Motion for Modification under *Fountain v. Filson*, 336 U.S. 681.

It is therefore obvious that the "law of this case", as relied on by appellant, cannot be that the net revenue clause is controlling. Otherwise the remanding of the case for a "further hearing in the court below" would have given rise to the exact situation which was eliminated by this Court's withdrawal of its first opinion.

Why was the case remanded for a "further hearing" in the District Court? It was remanded for the specific purpose of having the District Court rule on the admissibility of the evidence offered by Bradley in its Petition for Rehearing "*bearing on the meaning of the contract*" and, if the District Court found such evidence admissible, to interpret the contract in light of it.

This the District Court has done. It considered certain evidence previously discussed herein and interpreted the agreement in its light. The record of the pre-trial order and the trial demonstrates that a great deal of extrinsic evidence was offered and admitted—often without objection of counsel. Significantly, appellant has not urged that the evidence does not support the findings, and such a contention would not be tenable since the evidence overwhelmingly demonstrates the soundness of the findings and judgment.

This Court in its opinion raised the direct question "whether such extrinsic evidence is or would be admissible". *We submit that appellant has either misread or ignored the real determination of this Court.* Appellant states that "the determination of this Court of May 15, 1956 was controlling in the lower Court and is controlling in this appeal" (App. Op. Br. p. 12).

Appellant also takes the incredible position—"The trial court followed Bradley's contentions, disregarding the opinion of this Court dated May 15, 1956" (App. Op. Br. p. 10). Apparently appellant believes that the pre-trial in February 1957, and the trial in March 1957 before Judge Mathes were completely uncalled for. Appellant does not even attempt to meet this question of admissibility of the extrinsic evidence admitted in the District Court, nor has appellant cited any authority whatever as to why such evidence should not have been admitted. *Appellant merely asserts its plainly mistaken view that the issue of admissibility was not before the District Court.*

Yet Judge Mathes early in the trial clearly pointed out to counsel for United that he considered the contract ambiguous, particularly as applied to the later Yellow Pine Smelter construction by Bradley. He also referred to the matter of circumstances surrounding the execution of the 1941 contract and the question of admissibility (R. 98-99).

II.

APPELLANT HAS NOT PRESENTED ANY ISSUE TO THE COURT AND HAS NOT COMPLIED WITH THE RULES OF THIS COURT.

While we have no desire to be unduly technical, we respectfully urge that the method in which Appellant has presented this appeal leaves no issue to be decided by this Court.

First, in the "Statement of Points" required under this Court's Rules, Appellant merely enumerates certain findings of fact, conclusions of law and portions of the judgment, claimed to be in error (R. 447-450).

Second, in the brief, appellant's specifications of error are a verbatim repetition of the "statement of points" (Appellant's Op. Br. pp. 6-8). These specifications state no

reason why any of the findings are in error and thus violate Rule 18(2) (d) of the rules of this Court, which provides:

“* * * In all cases, when findings are specified as error, the specification shall state as particularly as may be wherein the findings of fact and conclusions of law are alleged to be erroneous * * *”

Third, the specifications are not stated separately; rather, each specification alleges more than one error. The first specification lumps no fewer than twenty alleged errors into one. “Specifications of error which set out more than one error are improper and need not be considered.” *Thys Company v. Anglo California National Bank*, 219 F.2d 131, 132 (9 Cir.); *Mutual Life Ins. Co. of N. Y. v. Wells Fargo Bank & Union Trust Co.*, 86 F.2d 585, 587 (9 Cir.).

Fourth, the points raised are not stated before being discussed; appellant’s “statement of issues” (Appellant’s Br. pp. 8-9) is merely another blanket assertion of error. Again this violates the rules⁷ and makes a clear understanding of appellant’s contentions difficult. The *Thys Company* case, *supra*, is applicable. In it this Court said (219 F.2d at 132, 133):

“Further, in disregard of the Rule, the particular points raised are not stated in full before being discussed, several allegedly erroneous findings of fact are joined under one heading for argument,⁸ and there is a failure to state with particularity wherein some of them are thought to be erroneous.”

(7) Rule 18(2)(c) of this Court provides that appellant’s brief shall contain:

“A concise abstract or statement of the case, presenting succinctly the questions involved and the manner in which they are raised.”

(8) In the present case appellant has joined *all* alleged errors under a single heading for argument.

We respectfully submit that such an almost complete disregard of this Court's rules justifies dismissal of the appeal. Again referring to the recent *Thys Company* decision (219 F.2d at 133):

“Where, as here, the brief for an appellant exhibits a gross disregard of the requirements of our rules, a dismissal of his appeal is warranted.”

Fifth, and perhaps most importantly, no issue as to whether the Court below properly admitted extrinsic evidence in interpreting the contract has been raised. Neither the specifications of error nor the statement of points claim that evidence was erroneously admitted, nor is there any reference to “the full substance of the evidence admitted”, to “the grounds urged at the trial for the objection” or to the transcript pages where such evidence appears, as required by Rule 18(2)(d) of this Court.

Thus, appellant's presentation creates the following situation: There is no issue as to whether evidence was properly admitted⁹ and we are even doubtful whether appellant intended to raise it since its brief does not give the substance of a single item of evidence which might be objectionable nor cite a single authority bearing on this issue. Appellant does not urge that the evidence does not support the findings, nor that the findings do not support the judgment. *There is therefore nothing before this Court except appellant's argument that the question as to which of the two clauses applied to the Yellow Pine Smelter were not to be decided by the Court below, despite this Court's explicit*

(9) This Court has so held many times under similar circumstances. E.g., *State of Washington v. United States*, 214 F.2d 33, 44; *Cly v. United States*, 201 F.2d 806, 809; *Lii v. United States*, 198 F.2d 109, 111-112; *Ziegler v. United States*, 174 F.2d 439; *Western Nat. Ins. Co. v. Le Clare*, 163 F.2d 337, 340; *Thys Company v. Anglo California National Bank*, *supra*; 14 *Cyc. Fed. Proc.* (3d ed.) 19.

direction to the contrary. This argument has already been considered.

The posture of the appeal constitutes a further reason for dismissing the appeal.

III.

EVIDENCE OF EXTRINSIC CIRCUMSTANCES IS ADMISSIBLE BECAUSE THE FACT THAT THREE COURTS HAVE REACHED OPPOSITE CONCLUSIONS ON THE MEANING OF THE CONTRACT SHOWS THAT IT IS SUSCEPTIBLE OF DIFFERENT MEANINGS AND THEREFORE AMBIGUOUS.

In *Salant v. Fox*, 271 Fed. 449, the Third Circuit said (p. 451):

"If we had been the first called upon to interpret this contract we should have regarded its language as clear and unambiguous, and and have construed it accordingly; but as the contract has been submitted to another court, it has given rise to three radically different interpretations, we must assume that its language is ambiguous and is susceptible of different meanings."

In *Davis v. Basalt Rock Co.*, 114 C.A. 2d 300, 250 P.2d 254 (hearing by California Supreme Court denied) it was said (p. 307):

*"We readily admit * * * that both sides frequently state that in many respects concerning the disputes between them, indeed in most, the contract was not ambiguous, but on the contrary clear, certain and not to be misunderstood. Nevertheless, each side claimed that the contract clearly declared in the way they interpreted it, and just as clearly excluded the meaning contended for by the opposing side. Such a situation is a familiar one. Such a situation also lends support to a determination that a contract capable of stating so clearly such opposite things is sufficiently ambiguous to justify the calling in of all permissible aids for its proper interpretation."*

And see the recent California Supreme Court case of *Beneficial Etc. Ins. Co. v. Kurt Hitke & Co.*, 46 C.2d 517, 524, 525, 297 P.2d 428:

“When the language used is fairly susceptible to one of two constructions, extrinsic evidence may be considered, not to vary or modify the terms of the agreement but to aid the court in ascertaining the true intent of the parties * * * not to show that ‘the parties meant something other *than* what they said’ but to show ‘what they meant *by* what they said’ * * *”

“The governing principle as to when parol testimony may be introduced to explain the language of a contract or to ascertain the intention of the parties is clearly set forth in *Kenney v. Los Feliz Investment Co., Ltd.*, 121 Cal. App. 378, 386, 387 [9 P.2d 225], as follows: ‘It is a settled rule that when the language employed is fairly susceptible of either one of two constructions contended for without doing violence to its usual and ordinary import an ambiguity arises where extrinsic evidence may be resorted to for the purpose of explaining the intention of the parties, and that for this purpose conversations between and declarations of the parties during the negotiations at and before the execution of the contract may be shown (*Balfour v. Fresno C. & I. Co.*, 109 Cal. 221 [41 P.2d 876]).’”

In the present case Circuit Judge Healy, sitting in the District Court, held that the contract on its face unambiguously meant what Bradley claims. This Court felt otherwise. Judge Mathes after pre-trial and trial reached the conclusion that the contract was unclear as to the main issue and rendered judgment for Bradley. The fact that the three courts differ shows that the contract is “sufficiently ambiguous to justify the calling in of all permissible aids for its proper interpretation” and therefore we submit that the

extrinsic evidence adduced and uncontradicted at the trial not only fully supports the findings and judgment here but also is clearly such a "permissible aid" for the proper interpretation of the contract.

Both intellectual humility and logic lead to this conclusion. The term "ambiguity" in the sense of the rule under consideration merely means that the contract is "susceptible of several significations", *Salant v. Fox*, supra; that it is "capable of being understood in more senses than one", *Whiting Stoker Co. v. Chicago Stoker Corporation*, 171 F.2d 248, 250, 251 (7 Cir.), or that the "language used is fairly susceptible of two constructions" or "any doubt exists", *Barham v. Barham*, 33 Cal. 2d 416, 202 P.2d 289; or, as stated in *Twin Falls Orchard & Fruit Co. v. Salsbury*, 20 Ida. 110, 117 Pac. 118, 122, "there is room for doubt", or, as stated in *Stone v. Bradshaw*, 64 Ida. 152, 128 P.2d 844, "different minds might well reach different conclusions". California law and Idaho law concur and control. Here the matter is not open to surmise. Different minds *have* reached different conclusions.

This Court similarly held in *United States v. Dollar*, 196 F.2d 551, where it reversed a summary judgment in a case turning on the meaning of a contract. The same contract had been in issue in *Dollar v. Land* in the District of Columbia, where the District Court construed the contract one way but was reversed by the Court of Appeals, which gave it a different construction. This Court said:

"The facts and circumstances before the courts in the case decided in the District of Columbia Circuit were such that reasonable minds not only could, but did, draw from them opposing inferences as to the nature and effect of the transaction. This being true the case was not one for summary disposition, but for trial and findings. Detsch & Co. v. American Products Co., 9 Cir. 152 F.2d 473".

UPON THE SLIGHTEST AMBIGUITY IN A CONTRACT, EXTRINSIC EVIDENCE IS ADMISSIBLE IN AID OF CONSTRUCTION.

Under *Erie R. Co. v. Tompkins*, 304 U.S. 64, "the interpretation of the contract" must be decided according to state law. *Transcontinental Air v. Koppal*, 345 U.S. 653, 656.¹⁰

This contract was entered into between an Idaho and a California corporation. The record is not clear as to the time and place of its execution. Depending on whether the latest signature was in California or Idaho, it is a California or Idaho contract. But it is immaterial which, for the law of the two states on construction of contracts is the same, and, as the Court knows, Idaho decisions pattern themselves on California law. Since the California cases on this subject are among the most articulate in the nation, the matter may be lucidly stated by quoting from them.¹¹

Usage and Custom

In *Body-Steffner Co. v. Flotill Products*, 63 C.A. 2d 555, 147 P.2d 84, which amasses the authorities on the subject

(10) This Court had previously so held in *William S. Gray & Co. v. Western Borax Co.*, 99 F.2d 239, 242 (9 Cir., per Denman, C. J.). Accord: *Edward B. Marks Music Corporation v. Foullon*, 171 F.2d 905, 908 (2 Cir.).

(11) For pertinent Idaho decisions see *Haener v. Albrow*, 73 Ida. 250, 249 P.2d 919, 925 (1952); *Williams v. Idaho Potato Starch Co.*, 73 Ida. 13, 245 P.2d 1045 (1952); *Stone v. Bradshaw*, 64 Ida. 152, 128 P.2d 844 (1944); *Twin Falls Orchard & Fruit Co. v. Salsbury*, 20 Ida. 110, 117 Pac. 118, 122 (1911); *Molyneux v. Twin Falls Canal Co.*, 54 Ida. 619, 35 P.2d 651, 654; *Wood River Power Co. v. Arkoosh*, 37 Ida. 348, 215 Pac. 975, 976, 977; *Caldwell State Bank v. First Nat. Bank*, 49 Ida. 110, 286 Pac. 360; *Johansen v. Looney*, 30 Ida. 123, 163 Pac. 303 (1913).

In *Williams v. Idaho Potato Starch Co.*, supra, a contract called for "a ten inch pump". As the Court said, this language was "clear on its face" but extrinsic evidence, if admitted, would show it to be in fact ambiguous:—"Upon the admission of this testimony, an ambiguity arises." The Court held the evidence admissible, and held further that "evidence of prior and contemporaneous negotiations" was admissible to remove the ambiguity.

and in turn is approved in *Union Oil Co. v. Union Sugar Co.*, 31 Cal. 2d 300, 188 P.2d 470, the Court succinctly stated two principles:

First (p. 558):

"It is a rule of practically universal acceptance in common law jurisdictions that however clear and unambiguous the words of a particular contract may appear on its face it is always open to the parties to the contract to prove that by the general and accepted usage of the trade or business in which both parties are engaged and to which the contract applies the words have acquired a meaning different from their ordinary and popular sense."¹²

Extrinsic Evidence Apart from Custom

Second, as respects "introduction of evidence, apart from evidence of trade usage" (p. 561-562):

"Where no extrinsic evidence is offered Courts are too frequently compelled to construe ambiguities and to reconcile inconsistencies by a consideration of the con-

(12) The Court here cited Civil Code, Sec. 1644; Code Civ. Proc., Sec. 1861; Rest., Contracts, Sec. 246(a); 2 Williston on Sales, 2d Ed., Sec. 618, p. 1556; 3 Williston on Contracts, rev. ed., Sec. 648, pp. 1871-2, Sec. 650, pp. 1874-9; 9 Wigmore on Evidence, 3d Ed., Sec. 2463, p. 204; 25 C.J.S., Customs and Usages, Sec. 24, pp. 111-2; 17 C.J., Id., Sec. 61, pp. 498-9; 12 Am. Jur. Contracts, Sec. 237, pp. 762-3; note 89 A.L.R. p. 1228 et seq.

The Restatement of Contracts, Section 246(a), comment, states "The rule * * * is not confined to unfamiliar words or to words often used ambiguously. Familiar words may have different meanings in different places. A usage may show that the meaning of a written contract is different from an apparently clear meaning which the writing would otherwise bear."

See decisions holding that every commercial contract is deemed to be entered into with the understanding that usage and custom in regard to the particular matter of the contract becomes a part of the transaction itself, unless the contrary appears: *Fischer v. First Nat. Bank of Sandpoint*, 55 Ida. 251, 40 P.2d 625; *Twin Falls Bank and Trust Co. v. Pringle*, 55 Ida. 451, 43 P.2d 515.

And see collected cases on usage and custom in recent case of *Beneficial Etc. v. Kurt Hitke & Co.*, 46 C.2d 524, 527; 297 P.2d 428.

tracts on their face; but where extrinsic evidence is offered to explain inconsistent provisions in a contract *Courts should not strain to find a clear meaning in an ambiguous document, and having done so exclude the extrinsic evidence on the ground that as so construed no ambiguity exists.* 'The true interpretation of every instrument being manifestly that which will make the instrument speak the intention of the party at the time it was made, it has always been considered an exception, or perhaps a corollary, to the general rule above stated, that when *any* doubt arises upon the true sense and meaning of the words themselves, or *any* difficulty as to their application under the surrounding circumstances, the sense and meaning of the language may be investigated and ascertained by evidence *dehors* the instrument itself.' "

This Court has ruled the same way, even in the days before *Erie v. Tompkins* established that state law must be followed on non-federal questions. Thus, in *Consolidated Coppermines Corp. v. Nevada C. Copper Co.*, 64 F.2d 440 (adopting opinion in 44 F.2d 192, cer. den. 290 U.S. 664), a mining case like the present, on the basis of extrinsic evidence this Court affirmed a judgment construing contract words, "all of the ore", to mean only all underground ore and not shovel-mined ore; i.e., that it did not in fact mean "all the ore".

The United States Supreme Court has long held that resort may always be had to the circumstances in which the contract was made. *Lowrey v. Hawaii*, 206 U.S. 206, 218, 219-222; *United States v. Bethlehem Steel Co.*, 205 U.S. 105, 117-118; *Harton v. Loffler*, 212 U.S. 397, 404.

In fact, there is a great body of outstanding authority that extrinsic evidence is always admissible whether a contract is ambiguous on its face or not. *United States v. Bethlehem Steel Co.*, *supra*, is noted in *United States v. Lennox Metal*

Manufacturing Co. 225 F.2d 302 (2 Cir. 1955), as so holding, as are California decisions, Corbin on Contracts and 9 Wigmore on Evidence (3rd Ed.), Sec. 2461, et seq.¹³ Thus Professor Corbin, in the latest and most thorough treatise on the subject, inquires whether "words (are) ever so 'plain and clear' as to exclude proof of surrounding circumstances and other extrinsic aids to interpretation" and doubts that they are (3 Corbin on Contracts, Sec. 542, p. 66). He states that cases so holding "should be subjected to constant attack and disapproval" because "it is easy to jump to a conclusion" (3 Corbin p. 71).

But without going so far, the Courts almost universally agree, in the language of the *Body-Steffner* case, that if there is the least sign of ambiguity, then extrinsic evidence should be admitted and that the Court should not strain to find absence of ambiguity. Thus in *United States v. Lennox Manufacturing Co.*, 225 F.2d 302 (2 Cir. 1955), it is said:

"* * * even those Courts which still say ambiguity is a

(13) The *Lennox* case states:

"The 'ambiguity-on-its-face' rule is a vestigial remain of a notion prevailing in 'primitive law' * * * (310)

"Even if a word in a written agreement is not ambiguous on its face, the better authorities hold that its context, its 'environment', must be taken into account in deciding what the parties mutually had in mind when they used that verbal symbol.

"The problem of interpreting a contract is, of course, that of understanding the communication between the parties * * * (310). Judge Learned Hand has sagely warned that, in attempting a solution, it is 'one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary * * * (311) * * * 'The law requires the Court to put itself as nearly as possible in the position of the parties, with their knowledge and their ignorance, with their language and their usage. It is the meaning * * * of the parties, thus determined, that must be given legal effect.' "

In *Body-Steffner Co. v. Flotill Products*, 63 C.A. 2d 555, 562, 147 P.2d 84, the Court similarly said:

"There is a considerable body of opinion among students of the subject whose conclusions are entitled to the greatest

necessary condition of considering such extrinsic evidence are quick to find such ambiguity, on slight grounds, when the extrinsic evidence is convincing.” (313)

In *Barham v. Barham*, 33 Cal. 2d 416, 202 P.2d 289, the Supreme Court of California sums up the rules of interpretation:

“Where *any doubt* exists as to the purport of the parties’ dealings as expressed in the wording of their contract, the Court may look to the circumstances surrounding its execution—including the object, nature and subject matter of the agreement (citation)—as well as to subsequent acts or declarations of the parties ‘shedding light upon the question of their mutual intention at the time of contracting’ (citation).¹⁴”

respect that parol evidence should always be admissible to show the sense in which the contracting parties used and understood the language of their written contracts.”

See also *Wells v. Wells*, 74 C.A. 2d 449, 169 Pac. 2d 23 and *Union Oil Co. v. Union Sugar Co.*, 31 Cal. 2d 300, 306, 188 Pac. 2d 470, which cites, in support of the view that “extrinsic evidence is generally admissible to show the sense in which the parties used language embodied in the contract, whether or not the words appear ambiguous to the reader”, *Universal Sales Corp. v. California etc. Mfg. Co.*, 200 Cal. 2d 751, 776, 128 P.2d 665; Rest. Contracts, Sec. 242, comment a; Holmes, *The Theory of Legal Interpretation*, 12 Harv. L. Rev. 417, 420; 9 Wigmore on Evidence (3d Ed.) Sections 2458-2478; McBaine, *The Rule Against Disturbing Plain Meaning of Writings*, 31 Cal. L. Rev. 145.

(14) Compare the recent decision of the Court of Claims in *Blackburn v. United States*, 116 F. Supp. 584, 586 (1953) where a summary judgment was denied, the Court saying:

“The language inserted in the contract is by no means so clear, *if language ever is so clear*, as to make inadmissible evidence as to what the parties to the contract intended it to mean. That intention, if it is mutual, is the essence of any contract, and the parties to it are privileged to use whatever form of shorthand, code, trade, ungrammatical, or other expression they may hit upon. They may make trouble for themselves and for a Court by their unorthodox expression, but they do not forfeit their rights.”

V.

PRACTICAL CONSTRUCTION OF CONTRACT BY THE PARTIES' CONDUCT.

No rule of interpretation is better settled than that the construction placed on a contract by the acts and conduct of the parties is entitled to great weight and will, when reasonable, be adopted and enforced by the courts. See *Beneficial Etc. Ins. Co. v. Kurt Hitke & Co.*, 46 C.2d 524, 527; 297 P.2d 428:

"To this latter point, it is said that 'a construction given the contract by the acts and conduct of the parties with knowledge of its terms, before any controversy has arisen as to its meaning, is entitled to great weight and will, when reasonable, be adopted and enforced by the court.' (*Woodbine v. Van Horn*, 29 Cal. 2d 95, 104 [173 P.2d 17] * * *)"

"It should be clear, therefore, that extrinsic evidence was admissible here as an aid in construing the contract. The meaning given by the parties to the contract since its existence and their performance thereunder, the preliminary negotiations and the question of whether custom and usage in the insurance business has given meaning to the terms of the contract are all relevant to the interpretation of it and should enable the trial court to ascertain the meaning of the contract."

See also *Barham v. Barham*, 33 Cal. 2d 416 at 423; 202 P.2d 289; *Tanner v. Title Ins. & Trust Co.*, 20 Cal. 2d 814, 823; 129 P.2d 383; *Cottle v. Oregon Mut. Life Ins. Co.*, 60 Ida. 628, 94 P.2d 1079; Williston on Contracts, Secs. 623, 629. Thus in *Frank v. Bauer*, 19 Colo. App. 445, 75 Pac. 930, the court said (p. 932):

"* * * the parties themselves construed the contract in this respect by paying royalty upon the value of the ore at the smelter, *less smelting charges*. They thus defined the meaning of the words 'mint or smelter returns,' and

this interpretation, in the absence of other evidence, we are justified in accepting."

(1) Boise Purification Plant.

Without any objection as to admissibility extrinsic evidence was introduced as set forth in the above statement of facts as to the erection by Bradley of its own purification plant in Boise. Tungsten concentrates derived from the ordinary mining process at the mining properties were processed through this plant at Boise in order to make them marketable. This operation continued from 1943 to 1945. The testimony is clear and uncontradicted that the type of treatment at the Boise Purification Plant was beyond the ordinary treatment processes normally applied by mine operators.

Bradley deducted its costs of operating this plant before calculating appellant's royalty on the proceeds. Its accounting to United showed exactly what it did, and appellant accepted the practice and accounting as proper (R. 142, 145, 152). *This was, as has been shown, the basis of accounting under the "net smelter returns method".*

This clearly demonstrates that United did not consider itself entitled to royalty on that part of the "amount paid by any purchaser" which was due to added value created by Bradley's activity and expenditures not within the ordinary treatment processes of a mining operation. This practical construction of the contract by the parties' conduct occurred *after* the 1941 contract. It continued for a two year period and before the erection of the Yellow Pine Smelter by Bradley at the property.

The whole Boise Purification Plant picture and accounting methods unquestionably show the conduct of the parties bearing on the construction of the contract as to the royalty provisions, and the propriety of Bradley's deduc-

tion of smelting charges and accounting to United on a *net smelter return* basis as to concentrates processed at Bradley's Yellow Pine smelter.

(2) The 1950 Contract.

As set forth in the statement of facts, the parties entered into an agreement on July 20, 1950 (R. 337-381). The uncontradicted evidence (R. 173-175), particularly as to recitals shows that the "royalties due" to appellant for the particular period mentioned were computed according to the *net smelter returns* method.

(3) No Objection to Computation of Royalties for Approximately Two Years After Smelter Construction.

The record is uncontradicted that no one representing United ever objected to the method by which Bradley had been computing royalties on materials that went through the Yellow Pine smelter, i.e., on the *net smelter returns method*—for a period of approximately two years (R. 178, 179).

VI.

THE CONSTRUCTION OF A CONTRACT IS PRIMARILY THE FUNCTION OF THE TRIAL COURT.

The function of an appellate court is merely to review such construction of a contract, not to act *ab initio*. After the introduction of evidence at a trial, the District Court reached a construction. On appeal from *that* judgment, this Court's task is to determine whether the evidence adduced, *added* to the face of the contract, was sufficient support for the decision, and to determine whether or not the findings are "clearly erroneous."¹⁵

(15) Rule 52(a) Federal Rules of Civil Procedure.

As said by this Court in *Hycon Manufacturing Company v. H. Koch & Sons*, 219 F.2d 353, 355 (9 Cir.):

“No authority is given except to District Courts to make new findings of fact. Presently our sole function * * * is to re-examine judicially, criticize and set aside if ‘clearly erroneous’. The existence of the basis of fact in documentary form or in agreed statement of the parties does not transmute such propositions into questions of law.”

In *Arnstein v. Porter*, 154 F.2d 464, 474 (2 Cir.), it was said that one must not

“convert an appellate court into a trial court. The avowed purpose of those who sponsored the summary judgment practices was to eliminate needless trials * * * In the attempt to apply that reform—to avoid what is alleged to be a needless trial in a trial court—we should not conduct a trial in this court. Where the facts are thus in real dispute, *it is our function, after a trial in the lower court, to review its legal conclusions and, with reference to its findings of fact, to determine not whether we would ourselves have made them, but merely whether they rest on sufficient evidence in the record* * * * in reviewing a judgment * * * ours must be a limited function. This is not, and must not be, a trial court. Such a court has a duty more difficult and important than ours.”

Construction of a contract with the aid of extrinsic evidence is a matter of inferences. Inferences are themselves facts, and a trial court’s findings thereon, like any other findings, are controlling unless clearly erroneous. *Walling v. General Industries Co.*, 330 U.S. 545, 550; *Tennant v. Peoria & P. U. Ry. Co.*, 321 U.S. 29, 35. This Court has said that “any attempt on the part of the appellate court to draw an inference of fact [contrary to one not clearly erroneous] constitutes a ‘usurpation of the province of the trial

court' ". *United States v. Fotopulos*, 180 F.2d 631, 635 (9 Cir.). And see *Estate of Bristol*, 23 Cal. 2d 221, 143 P.2d 689, and *Estate of Rule*, 25 Cal. 2d 1, 152 P.2d 1003, where it is said that an appellate court may not supplant the trial court's interpretation of a contract where extrinsic evidence has been received which permits diverse inferences.

The Supreme Court's Advisory Committee praises this Court's decision in *Quon v. Niagara Fire Ins. Co. of New York*, 190 F.2d 257 (9 Cir.)¹⁶ where it was aptly said:

"The writing under these circumstances must be viewed in its setting together with all the other evidence in light of the credibility accorded the witness. Here the writing is one of the collateral facts. * * *"

"Under such circumstances, the use of the cliché that the appellate court is in as good a position as the trial judge to construe a writing is futile. The maxim is not true, as often happens with stereotyped sayings, in this situation. Here the construction entered into a finding of fact which cannot be set aside unless clearly erroneous. *In attributing imperative influence to a writing, courts would be reverting to the authoritarian doctrine of medieval scholasticism.* Wigmore's language made a destructive criticism of this view: '* * * a writing is, of itself alone considered, nothing,—simply nothing. It must take life and efficacy from other facts, to which it owes its birth; and these facts, as its creator, have as great a right to be known and considered as their creature has. * * * There is no magic in the writing itself. It hangs in mid-air, incapable of self-support, until some foundation of other facts has been built for it.' 9 Wigmore on Evidence, 3rd Ed., 5."¹⁷

(16) Report of October 1955, p. 53, comment under proposed amendment to Rule 52.

(17) Numerous other decisions of this Court can be cited on the limited function of an appellate court. E.g., *Waiialua Agr. Co. v. Maneja*, 178 F.2d 603; *Helbush v. Finkle*, 170 F.2d 41; *Paramount Pest Control Service v. Brewer*, 170 F.2d 553; *Jacuzzi Bros. v. Berkeley Pump Co.*, 191 F.2d 632, 637.

property included a cyanidation plant to produce gold bullion to be sent to the U. S. Mint.

Prior to 1939, the property was known to contain **mercury** (quicksilver or cinnabar). Again the record shows that the *cinnabar ore is not sent to a smelter*—the crushed ore is merely roasted or furnaced to produce the metal mercury (quicksilver).

The evidence has shown that, in the industry, “mining” is understood to include every step from the extraction of ore through crushing, milling, concentrating and some simple treatment processes. *But it has never been deemed to include smelting.* As reflected in the 1939 Internal Revenue Code, and as testified to, the miner commonly owns and operates a mill and concentrator, but he almost never owns or operates the smelter. *Crushing and concentrating are “ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product.” Smelting is not.*

Section 114(b)(4)B of the Internal Revenue Code of 1939¹⁹ specifically defines income from mining property in reference to depreciation and depletion allowances. The parties discussed depletion prior to execution of the 1941 contract. We quote:

“As used in this paragraph the term ‘gross income from the property’ means the gross income from mining. The term ‘mining’, as used herein shall be considered to include not merely extraction of the ores or minerals from the ground but also *ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketably mineral product or products*, and so much of the transportation of ores

(19) We quote the Internal Revenue Code of 1939 because it was the text in effect when the contract was made. The comparable provisions of the Internal Revenue Code of 1954 are in Section 613(c) and are the same except for paragraphing.

or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto. * * * The term 'ordinary treatment processes' as used herein shall include the following: * * * (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (*but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining*), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, **including the furnacing of quick-silver ores.**"

The simple fact is that a pound of metal content in a mass of concentrates is not worth the same as a pound of refined metal as it comes from a smelter. The value of the refined metal is composed of two elements, (1) the value taken from the mining property, and (2) an additional value imparted to it by the smelter in refining it at the cost of labor, power, supplies and investment of capital.

The words "net revenue from the properties" or "values from the properties" cover element No. 1. They cannot include element No. 2.

(2) Purpose of Net Revenue Provision.

The record now shows the emphasis on a *market*—the sources of revenue on which royalties would be computed. As has been shown, the market is sometimes a mint and sometimes a smelter. It is also *uncontradicted that the "net revenue" clause has and was intended to have a "catch-all"*

application to various situations where smelting is not involved.

It will be recalled that in the Fall of 1941 and prior to the execution of the December 31, 1941 agreement, substantial sales of unsmelted tungsten concentrates were made to purchasers and consumers. It is now clear from the record that under the circumstances the parties were defining a marketing situation which did not involve the smelter process. The emphasis on the *market* is also seen in the contract itself (R. 17, 18) where the sources of revenue are referred to three different times as "smelter, *market* or mint."

The circumstances as to how the "net revenue" clause was placed in the contract and the reasons therefor have already been set forth in reference to the uncontradicted testimony. The parties at the time knew of the various materials extracted from the properties that would not have to be subjected to the "extraordinary" process of smelting, *i.e.*, "*we were hunting for a clause that would cover products that would not go to a mint, such as gold bullion, or sulphide concentrates that would go to a smelter.*"

Certain closely analogous situations may be noted. In *Helvering v. Bankline Oil Co.*, 303 U.S. 362 (reversing this Court), the Supreme Court refused to allow a percentage depletion based on the entire proceeds from the sale of casinghead gasoline. Only part of the value came from the "mining". The rest was from refining.²⁰

(20) *Danciger Oil etc. Co. v. Hamill Drilling Co.*, 171 S.W. 2d 321, 141 Tex. 153, "involved the construction of an oil and gas mining contract". Buying an oil lease interest, Danciger promised to pay a certain percentage "of all the oil, gas, casinghead gas and other minerals produced, saved and marketed * * * from the properties * * * *free and clear of operating expenses* * * *" Then Danciger built an absorption of distillation plant on the premises to separate the gas into its component parts. The issue was whether the royalty was to be paid on the receipts of the products manufactured from the gas, without any deduction for the cost of processing

VIII.

THE NET SMELTER RETURNS PROVISION

At the outset, we saw that the issue of contract construction is this:

Is United to get the same royalty when the concentrates go through a smelter owned by Bradley on the premises as if they went through an independently owned smelter, *or is it to get a greater royalty merely because the smelter is owned by Bradley?*

(1) United's Construction Writes Words into the Contract.

Under Bradley's interpretation, the word "smelter" in the phrase "net smelter returns" encompasses *any* smelter. United's construction writes into the phrase the words "independently owned" or "third party owned" so as to make it read "net independently-owned smelter returns". The contract defines "net smelter returns" thus (R. 17):

"By *net smelter returns*, as used herein, is meant the amount received from *the* smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that *the* smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted."

United's construction changes the phrase "amount received from *the* smelter" to the phrase "amount received from *any independently owned smelter*".

This Court's opinion *also* writes in words, by saying that the "net smelter returns clause" is "by its terms * * * lim-

the gas into gasoline and other products. The Supreme Court of Texas, reversing the lower Courts, held no, stating (p. 322) that the royalty owner was not entitled to a share of the values added by a manufacturing process.

To the same effect is *Armstrong v. Skelly Oil Co.*, 55 F.2d 1066 (5 Cir.).

ited to situations where the 'amounts are received [by Bradley] from [outside] smelters.'” Those words in brackets are not in the contract.

In *Union Oil Co. v. Union Sugar Co.*, 31 Cal. 2d 300, 188 P.2d 470, the trial court had held that on its face a contract calling for certain action should be read as if it contained the words “in any event”. The Supreme Court of California reversed, observing (p. 306):

“Once something had to be read into a contract to make it clear, it can hardly be said to be susceptible of only one interpretation. It would have been error for the trial court to read something into the contract by straining ‘to find a clear meaning in an ambiguous document, and having done so exclude the extrinsic evidence on the ground that as so construed no ambiguity exists.’ (*Body-Steffner Co. v. Flotill Products*, 63 C.A. 2d 555, 562 [147 P. 2d 84].)”

(2) United's Construction Makes the Entire "Net Smelter Return" Clause a Superfluity.

United contends that no smelter charges are deductible where Bradley owns the smelter because it is the “net revenue” clause that then applies. The reasoning behind this contention is that where Bradley owns the smelter it “receives” nothing from the smelter and so there are no “smelter returns”.

But this construction reads the “net smelter” provision completely out of the contract as wholly superfluous.

Extracted from their matrix in industry usage, the phrases “smelter charges” and “net smelter returns” connote that a commercial or independently-owned smelter engages in the business of performing a service job for which it charges a toll or fee, returning to the owner of the concentrates the refined material less the charge for the service of refining. But the extrinsic evidence shows the

custom that independent smelters do "not charge a fee for performance of a service" and that, instead, they buy the concentrates and pay a purchase price. The concentrates become the property of the independent smelters (Finding XIII, R. 44).

Thus what is "received" from an independent smelter is simply *revenue*. If the "net smelter returns" clause is confined to independently owned smelters, that clause becomes a superfluity, for it adds nothing whatever to the "net revenue" clause, quoted above. Exactly the same revenue would be paid to United under the "net revenue" clause on concentrates going to an independent smelter as under the "net smelter returns" clause. But it is elementary, in every common law jurisdiction, that

"The whole of a contract is to be taken together, so as to give effect to every part, if reasonably practical, each clause helping to interpret the other." (Cal. Civ. Code, Sec. 1641. Cf. Restatement of Contracts, Sec. 235 (c)).²¹

In order, then, for the "net smelter returns" clause to have any office or function, it must apply to a smelter owned by Bradley.

(3) United's Construction Writes Out of the Net Smelter Return Clause a Significant Part.

Let us quote again the "net smelter return" clause. It reads (R. 17):

"By *net smelter returns*, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a

(21) Accord: 3 Williston on Contracts 1779 (Rev. ed. 1936); 3 Corbin on Contracts 100 (1951); *Bratton v. Morris*, 54 Ida. 743, 37 P.2d 1097, 1100 (1934); *Molyneux v. Twin Falls Canal Co.*, 54 Ida. 619, 35 P.2d 651, 653 (1934); *Caldwell State Bank v. First Nat. Bank*, 49 Ida. 110, 286 Pac. 360, 362 (1930).

smelter, *it being understood that the smelter will deduct its normal smelting charges* and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted."

Note the words, "it being understood that the smelter will deduct its **normal** smelting charges". If the "net smelter returns" clause applies only when the smelting is done by an independent smelter, these words are superfluous, for the amount received from the smelter is what it will pay. *Its* "deductions" would not be in the control of the parties.

The extrinsic evidence shows how these words got into the contract.²² In 1939 the parties entered into an option agreement, in which the "net smelter clause" first appeared. At that time the parties contemplated the possibility of a smelter on the property, for the same option agreement, in the very sentence preceding this definition of net smelter returns, refers to the possibility of "local reduction of the concentrates." Early drafts contained the clause "it being understood that the smelter will deduct its smelting charges". This addition, as to "*normal*" smelting charges, *is appropriate to the situation of a smelter operated by appellee. And this is underscored by the fact that the early drafts did not contain the limiting adjective "normal" before "smelter charges".* The final insertion of the word "normal" was to protect appellant against appellee charging for smelting more than independent smelters were accustomed

(22) "A contract may be explained by reference to the circumstances under which it was made * * *" (Cal. Civil Code, Sec. 1647). "For the proper construction of an instrument, the circumstances under which it was made * * * may also be shown, so that the judge be placed in the position of those whose language he is to interpret." (Cal. Code of Civil Procedure, Sec. 1860). These provisions are not merely California law, they are law generally. Restatement of the Law of Contracts, Sec. 235(d) ; 3 Williston on Contracts 1780 (rev. Ed. 1936) ; 3 Corbin on Contracts 17 (1951) ; Rudeen v. Howell, 71 Idaho 365, 283 P. 2d 587, 589 (1955) and cases cited therein.

to do in the industry. This is completely borne out by the record.

Judge Mathes, we submit, has aptly summarized the significance and application of the net royalty clauses (R. 250):

“It is my view that the Plaintiff’s construction would read the net smelter returns provision out of the contract, since the net revenue clause is general and covers everything not otherwise covered. If the net revenue clause is not the general catch-all then there is no explanation for having the mint and the smelter returns clauses in the contract, they are specific and appear to limit or control the general,—by the net revenue is meant the amount paid by the purchaser from the sale of concentrate, any purchaser. It is broad enough, as pointed out this morning, to cover whatever is covered by the net mint returns and whatever is covered by the net smelter returns. In any event, the plaintiff’s construction would read out of the net smelter returns clause the phrase, it being understood that the smelter will deduct its normal smelting charge and charges for railroad, freight, and so forth,—it wouldn’t read out the freight provision, of course, but it would read out the smelting charge provision, or it would necessarily read into the clause the words ‘third-party owned smelter’, or something of like effect. If the smelter was not owned by one of the parties to the contract then it had to be a third-party owned smelter.”

(4) In Industry Usage "Net Smelter Returns Received" Means Returns "Realized".

United has contended in this case that the “net smelter clause” refers to “net smelter returns *received*”, that the word “received” connotes payment by a third party, and therefore that the “net smelter” clause is not applicable to a smelter owned by appellee. And that is also suggested in this Court’s opinion of May 15, 1956.

We therefore note a contrast on the face of the writing that calls for explanation by extrinsic circumstances. The three definitions, of "net smelter returns", "net revenue" and "net mint returns", appear consecutively (R. 17). Net revenue is defined as "the amount *paid by any purchaser*"; net mint returns are defined as "the amount *paid*" by a mint. Thus where the parties meant to refer to a purchase price *paid* by a third party, they knew how to say so explicitly. Yet, in the same context, in speaking of smelter returns, they do not say "amount paid by the smelter". They say "amount *received* from the smelter." The deliberate change in language must and does have a significance.

The explanation of the significance here, as elsewhere, lies in industry usage.

As long ago as 1898 and 1903, in Colorado, it was held that "smelter returns" in a royalty contract mean "return from the ore, less the smelting charges." *Frank v. Bauer*, 19 Colo. App. 445, 75 Pac. 930, 932.²³ and in *Maloney v. Love*, 11 Colo. App. 288, 52 Pac. 1029, the court said of the words "net proceeds from all smelter * * * and mill returns"

"every miner and every person familiar with transactions involving leases of mining property knows exactly what they mean. They mean that * * * charges for treatment are to come out of the gross mill or smelter values, and what is left is net proceeds."

In short, the uncontradicted evidence of industry usage shows that "net smelter returns received" do not imply payment by a third party. The evidence is that these words are used in the industry to signify the net *realization* after smelting, whether by way of cash paid or credit given.

In the past, United's reasoning has been that where Brad-

(23) The court there commented that evidence of "any custom defining the meaning of these words" would be admissible.

ley owns the smelter it "receives" nothing from the smelter and therefore there are no "smelter returns". The uncontradicted testimony as to the custom and usage in the mining industry fully refutes this reasoning (R. 129, 130).

The stipulation by the parties (R. 426) as to the custom of accounting where the smelter and the mine are under the same ownership, we submit, gives complete validity to the manner of accounting followed by Bradley.

It is uncontradicted that Bradley in its computation of royalties from the Yellow Pine smelter operation made its accounting to United on the same basis as an independent smelter—which actually resulted in a benefit to United (See the fully supported Findings of Fact, XLI at R. 61):

"That the defendant has computed and paid royalties to the plaintiff upon products of the mine treated and processed by the defendant at the Yellow Pine Smelter on the same basis and utilizing the same treatment schedule, but without deducting freight charges, as in the case of identical concentrates shipped to outside smelters; the net effect being that plaintiff benefited in royalty payments when identical concentrates were smelted by the defendant at the Yellow Pine Smelter as compared with the best arrangement that could be made with an independently owned smelter; and the plaintiff did not object to the payment of such royalties by the defendant upon the basis of 'net smelter returns' until 1951."

IX.

CONTEMPLATION OF BRADLEY SMELTER

And now let us quote again the smelter royalty provision which is not mentioned in this Court's opinion nor in United's opening brief. Yet this is a key clause in the light of the uncontradicted testimony (R. 18).

"Should a smelter or other reduction works be erected between the mining property herein conveyed

and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works."

In the light of the record, this paragraph would now read: "Should a *Bradley* smelter be erected * * * *there shall be deducted from the net smelter or reduction returns* a fair charge for trucking * * *".

This is also the clue in the other net smelter returns provision—"it being understood that **the** smelter will deduct its normal smelting charge" i.e. whether **the** smelter is an outside smelter or owned by Bradley.

The extrinsic evidence shows how these words got into the contract.²⁴ It will be further noted that the contract of 1941 contains a provision relative to *trucking costs* "should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho". In that event "there shall be deducted from the net smelter or reduction returns *a fair charge for trucking* from the mine to such smelter or reduction works" (R. 18). The phraseology is noteworthy. It does not merely allow the deduction of a trucking charge; *the deduction is to be from the "smelter returns"*.

Again, it is now clear that the smelter in contemplation in 1941 was *only* a Bradley smelter. Thus, spelling out the provision in the light of the uncontradicted testimony, the clause reads

"* * * Should a **Bradley** smelter be erected * * * *there shall be deducted from **Bradley's** net smelter or reduction returns* * * * *a fair charge for trucking* * * * from the mine to **Bradley's** smelter or reduction works."

United's claimed construction is also contrary to the admitted purpose in making the change in contracts. The pur-

(24) See Footnote 22, *supra*.

pose of Bradley was to obtain a reduction of the 1939 contract royalty rates; the purpose of United in agreeing to lower royalties was to make it economically feasible for Bradley to mine low grade ore. United's construction runs directly counter to the avowed reasons for the change to the 1941 contract (Finding XXVI, R. 52).

We believe we need make no further comment on the uncontradicted testimony as to the construction of the contract by the conduct of the parties.

CONCLUSION

In this action a summary judgment for Bradley was reversed by this Court and the case was remanded to the District Court for the specific purpose of a hearing of extrinsic evidence—offered by Bradley in its Petition for Rehearing and Modification—as “bearing on the meaning of the contract.” This Court's direction was therefore that a trial be had on the merits as to the construction of the contract subject to the rules as to admissibility.

The record of uncontradicted testimony, we submit, goes even beyond Bradley's offer of proof referred to in this Court's opinion. Extrinsic evidence was introduced, received as admissible testimony—was uncontradicted—and stands without rebuttal. It is submitted that the extrinsic evidence not only fully supports the findings and judgment but is clearly a “permissible aid” to the proper interpretation of the contract, pursuant to the authorities cited herein.

APPENDIX

DISTRICT COURT COMMENTS FROM BENCH AFTER TRIAL AND ARGUMENTS OF COUNSEL

The Court: The contract is admitted and the salient features that we are involved with are, of course, as set forth on pages 15 to 18 of the record on appeal, which is excerpted from Exhibit Seven here.

We bear in mind that the contract was made in 1941 and the smelter built in 1949. Our problem here is to ascertain the intention of the parties as manifested by the writing when read in the light of the facts and circumstances in evidence surrounding execution. The controversy arises, of course, because the contract is unclear as applies to this subsequently constructed smelter operation on the property, although admittedly the contract contemplated the possibility. It did not literally in so many words cover the contingency of the smelter on the property owned and operated by one of the parties to the contract.

It is stipulated, of course, at Q on Page six of the Pre-trial Conference Order: "That, if under the terms of the contract, defendant, Bradley Mining Company, is entitled to make any charge or deduction for smelting ores in the Yellow Pine Smelter, the charges and deductions so made by Bradley Mining Company have been proper charges and deductions, and all settlements made with the plaintiff have been correct."

"If it is ultimately determined that the net smelter returns provisions of the agreement is applicable to the operations of the Yellow Pine Smelter for ores, concentrates, metals and values taken from the claims described in the agreement, then the settlement made by Bradley have been correct as to the minerals, ores, metals and value processed at the smelter."

“That there is no dispute as to the meaning and interpretation of the net mint return clause of the contract.” That appears under R, at the top of page seven of the Pretrial Conference Order.

I find that this contract was made by experienced mining people, including the principal draftsman,—I say principal, at least it appears in the record to be a fair inference that Mr. Worthwine was the principal draftsman, and a party interested in the contract, and the performance of it as it turned out, so I find that the parties contracted with reference to the practices and customs in the mining industry prevailing at that time and as they envisioned such might be over the years. I think one significant fact that we may be inclined to forget at times, and one that should be kept constantly in mind, these parties envisioned this arrangement to last for ten centuries. That is a bold undertaking. I would hate to be called upon to envision what may be going on in the mining industry in the year 2000, much less the year 2900 and something, nine centuries later, but it is admitted under S, at Page seven of the Pretrial Conference Order: “That before 1939 and thereafter at all times material to this action, it was the practice and custom in the smelting industry for companies who own and operate smelters to also own and operate mines; that it was likewise the practice and custom in the industry for companies owning mines and also owning smelters to ship their mine produce to their own smelters; that it was likewise the practice and custom with respect to owners of smelters and mines, to also lease mining properties from other independent owners, and send the produce extracted therefrom to their own smelters and to settle for the product so shipped on the same basis as such smelting companies would settle with independent or custom shippers; that it was a practice

and custom of the trade that where the ores treated came from mines owned by the owners of smelters, or came from mines leased and mined by the smelter owner or came from independent custom shippers, that the smelting charge and the cost of transportation of concentrates to the smelter were deducted to arrive at a net amount commonly referred to in the mining and smelting industries as net smelter returns."

Under T on Page seven it is stipulated: "That it is a matter of common knowledge and historically recognized in the mining industry that the milling of ores to reduce such ores to a concentrate form is a part of the mining process, and that the smelting of ores is not a part of the mining process."

There has been evidence of other customs and practices in the mining industry, that evidence stands uncontradicted. The other surrounding facts and circumstances siding in the interpretation are the 1939 agreement, Exhibit 5, and the provisions of that agreement, and it is uncontradicted that one of the purposes of the 1941 agreement was to reduce the amount of royalty required to be paid by the defendant, and, as it has been developed here in our discussions today, the defendant's purpose to get a reduction in royalty, for obvious economic reasons the plaintiff was moved to grant it because the plaintiff's purpose thereby was to induce defendant to a more intensive mining of the ores, particularly the low-grade ores on the property, or which might thereafter be found on the property. Having in mind again that this five percent arrangement was to last for a thousand years and even longer if paying values were found. As I have said before, it is uncontradicted that the possibility that the defendant might build a smelter at the site of the mine was discussed during the negotiations of the 1941

contract, and it is admitted that under P of the Pretrial Conference Order at Page six: "That at the time of the execution of the contract, December 31, 1941, there were no smelters located at Cascade, Idaho." The contract itself, as was developed this morning envisages the possibility of a smelter near the mine and it was conceded in argument that that referred to the possibility that the defendant itself might build a smelter at or near the mining property. The provision in question appears at Page 18 of the Transcript of the record, and reads: "Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the *net smelter* or reduction returns, a fair charge for trucking from the mine to such smelter or reduction works."

I have already referred to the custom and practice with respect to the operation of smelters. The parties contracted in the light of that practice. There is uncontradicted evidence that tax problems were discussed during the negotiation of the 1941 agreement, including the problem of depletion, and it seems a fair inference that the parties did contract with respect to these tax problems existing and possibly contemplated for the future end, of course, it will be assumed that they contracted with reference to existing laws. The Internal Revenue Code of 1939 at that time, specifically Section 114 (b) (4) (B) made provision for depletion allowances computed upon gross income from the property to mean the *gross income from mining*. The Statute defined the term "mining", "to include not merely the extraction of the ores or minerals from the ground but also the *ordinary* treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by

common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto", and then the statute proceeds and defines the ordinary treatment processes incident to mines, and states: "The term 'ordinary treatment processes', as used herein, shall include the following", in the case of many minerals, including gold and silver, "which are not customarily sold in the form of crude mineral products,—crushing, grinding and beneficiation by concentration, such as gravity, flotation, amalgamation, electrostatic, or magnetic, cyanidation, leaching, crystallization, precipitation (*but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining*)", and continuing "or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores." The statute thus attempts to define the ordinary treatment processes normally applied by mine owners in order to obtain a commercially marketable mineral product. Of course, when that product is obtained, that is the point at which the computation must begin for the purposes of depletion, or to put it another way, in computing the gross income from mining an operator may not proceed beyond these ordinary treatment processes, or he may not count the income,—beyond the ordinary treatment processes normally applied in order to obtain a commercially marketable product. Thus, in the case of *Helvering v. The Bankline Oil Company*, 303 U.S., Page 262, that was a case in which the Court refused to allow the depletion based on the sale of the end product because that included some refining processes beyond the ordinary treatment processes normally applied.

In addition to the surrounding circumstances there is certain conduct of the parties subsequent to the 1941 agreement, which throws light upon the intention of the parties,

and that is this question of the tungsten ore, the uncontradicted evidence is that the tungsten ore was subjected to a flotation process at the mine, and it is interesting to note that the flotation process is included among the ordinary treatment processes by the mine owners in the statute that I just referred to of the Internal Revenue Code. These concentrates resulting were sold in the eastern market direct from the mine, reports were made, and royalty paid accordingly under the net revenue clause. Then there were certain tungsten concentrates that were sent to the defendant's Boise purification plant, and with respect to those, the net smelter return method of computing royalty was used. Then there is the question of recitals in the 1950 modification agreement, Exhibit Number 6, which appears at Page 69 of the record transcript, in more particular the recitals with respect to May, 1950, royalty, which the uncontradicted evidence shows were computed according to the net smelter returns method.

I find that the parties, having in mind that this agreement was to last for such an unusually long period of time, that they envisioned, not only the possible method of marketing the mine product from the property, but also the possible variety of the minerals which possibly would be produced and marketed in the future, including gold, silver, antimony, tungsten, quicksilver and so forth, and as I read the provisions in question and particularly the provision commencing at Page 15 of the Transcript of the record, Exhibit Number 7, the 1941 Agreement, we first find that there is a five percent royalty promise on all net smelter returns, net revenue, and net mint returns, as defined herein; and then over on Page 17 we find that net smelter returns are defined, net revenue is defined, and net mint returns defined. Then, reading on through the provision with respect to transportation, we find that the parties refer to the three methods,

I shall call them, handling returns. Referring to those methods as net smelter, market or mint returns. Smelter, market or mint,—net smelter, market and mint returns, smelter, market or mint, to which the same are trucked and so forth. The emphasis upon market is persuasive in the light of all of the other circumstances, that the parties have in mind here possible marketing methods, envisioning the possibility over the years, so they, as to anything marketable, in a condition to be marketed, the mint,—at the time they contracted the mint was the market. As to anything required to go to the smelter, the smelter was the market. As to other matters, as to concentrates, ores, metals or values, the net revenue provision was intended as a catch-all,—another method of marketing direct from the property. In other words, by transporting the product directly from the mine to the mint whenever the quality would permit such a relatively simple operation; by sending it to the smelter to be processed in the customary way, and in the third place, by marketing ore concentrates and values direct to third persons from the mine, after the mining process had been completed. This evidence of custom and practice and other surrounding circumstances and subsequent conduct is not contradicted, nor is it otherwise illumined by any testimony from either Mr. Worthwine or Mr. Oberbillig.

It is my view that the Plaintiff's construction would read the net smelter returns provision out of the contract, since the net revenue clause is general and covers everything not otherwise covered. If the net revenue clause is not the general catch-all then there is no explanation for having the mint and the smelter returns clauses in the contract, they are specific and appear to limit or control the general,—by the net revenue is meant the amount paid by the purchaser from the sale of concentrate, any purchaser. It is broad enough, as pointed out this morning, to cover whatever is

There is no necessity under this view of the agreement to require an accounting and that will not be required.

The Court will rule that each party bears its own costs, and the Findings of Fact and Conclusions of Law and Declaratory Judgment will be prepared by counsel for the defendant.

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(Endorsed) : Filed July 16, 1957

No. 15652

IN THE
United States
Court of Appeals
For the Ninth Circuit

UNITED MERCURY MINES COMPANY,
Appellant,
vs.
BRADLEY MINING COMPANY,
Appellee.

BRIEF OF APPELLANT

*Appeal from the United States District Court
for the District of Idaho, Southern Division*

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FILED

MAY 5 1957

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UNITED MERCURY MINES COMPANY,
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BRIEF OF APPELLANT

*Appeal from the United States District Court
for the District of Idaho, Southern Division*

*This is an appeal from the United States District
Court for the District of Idaho, Southern Division,
upon rehearing ordered in this case.*

STATEMENT OF THE CASE

This is an action brought by the plaintiff United Mercury Mines Company, hereinafter called "United" against Bradley Mining Company, hereinafter called "Bradley" for an accounting of royalties due under a written contract dated December 31, 1941 in which the plaintiff sought an interpretation of

the provisions of the contract and the proper and legal method of determining the amount of royalty due for values extracted and smelted at the Yellow Pine Smelter. Under the contract of December 31, 1941 (R. 12) United conveyed to Bradley certain mining claims in Valley County known as the Meadow Creek Group and the Hennessey Group, and in consideration thereof Bradley agreed to pay United "a royalty of five per cent (5%) on all net smelter returns, net revenue, and net mint returns, as defined herein, upon and for all minerals, ores, metals or values, of any and every kind and character, mined, extracted or taken from the --- mining claims, or any part thereof." (R. 15)

The parties defined net smelter returns, net revenue, and net mint returns as follows:

"By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges and charges for railroad freight from Cascade, Idaho, to said smelter shall also be deducted.

"By net revenue, as used herein, is meant the amount paid by any purchaser from the sale of concentrates, ores, metals or values shipped, taken or produced from said properties, less marketing and shipping costs from Cascade, Idaho.

"By net mint returns, as used herein, is meant the amount paid by any United States Mint, Branch or

agency thereof, less all shipping and marketing costs from Cascade, Idaho.”

The payment of the royalty for all minerals, ores, metals, or values, hereinafter called “values” was to continue for a term of 999 years and so long thereafter as values may be extracted from the said mining claims. (R. 16)

In the performance of said contract, United, by and through sufficient conveyance, transferred to Bradley the claims constituting the Meadow Creek and Hennessey so that title to the said claims and all values therein vested absolutely in Bradley. (R. 409, 413)

In 1949 Bradley, at its own costs, constructed the Yellow Pine Smelter upon the said claims and thereafter proceeded to smelt therein its own concentrates produced from the said claims and thereafter sold quantities of their own smelted products to certain purchasers. (R. 409, 413)

The Yellow Pine Smelter was at all times solely owned by Bradley which operated the same at its own expense in the reduction of its own values. (R. 409, 413)

After the construction of the Yellow Pine Smelter approximately 55%, based on values, of the so owned concentrates were treated at the Yellow Pine Smelter and after completion of the smelting process certain of the products were sold to purchasers. (R. 400, 406)

As to the products from the Yellow Pine Smelter,

originating from the said mining claims, Bradley did not compute and pay royalties to United under the provisions of the net revenue clause, on the amount received from the sale of the end products (R. 412, 416), but computed and paid royalties under its own interpretation and its own application of the net smelter returns clause to the concentrates at the mouth of the smelter, without having received any amount of money whatever from any source whatever for the said concentrates.

Although Bradley has sold to purchasers certain salable products resulting from its operation of the Yellow Pine Smelter, which found origin from the said mining claims, it has not paid United any sums equal to 5% of the amount received by Bradley from the purchasers. (R. 412, 416)

That at the time of the erection or construction of the Yellow Pine Smelter there were no smelters located at or near Cascade, Idaho, or between Cascade, Idaho, and these mining properties.

To United's complaint (R. 3-26) Bradley filed its answer (R. 26-35) and on such complaint and answer, affidavits and interrogatories and answers thereto, all of which appear in the transcript of record on appeal of this court, No. 14750 the matter came on for pre-trial hearing on February 1, 1955, as a result of which a judgment of dismissal was entered in favor of Bradley and from which appeal was taken by United to this court on February 21, 1955. That on February 8, 1956 this court entered its opinion herein as Case No. 14705, which

opinion was subsequently modified by this court's opinion filed May 15, 1956 and now reported in 204 F. 2d 205, which opinion reversed the lower court and remanded the matter to the District Court. Thereafter, on March 19, 1957, the matter came on for trial before the Hon. Wm. C. Mathes, sitting without a jury and findings of fact, conclusions of law and judgment were entered therein on April 20, 1957, from which judgment appeal was taken to this court on May 20, 1957, and on the same day a cost bond filed. (R. 67-68)

The lower court's judgment of April 20, 1957 held inter alia that the net revenue provisions of the contract did not apply as contended by United, but that the net smelter provisions of the contract did apply as contended by Bradley with reference to minerals, ores, metals and values extracted from said mining claims and smelted at the Yellow Pine Smelter.

JURISDICTION

Jurisdiction of the District Court is based upon diversity of citizenship, United being a citizen of Idaho and Bradley being a citizen of California (R. 3, 27), and the amount in controversy, which exceeds, exclusive of interest and costs, the sum of \$3,000.00 (R. 10). Title 28, Section 1332, United States Code.

This court has jurisdiction to reverse the case on appeal by reason of Title 28, Section 1291 and 1294, United States Code and Rule 73 of the Federal Rules of Civil Procedure.

SPECIFICATIONS OF ERROR

I. The court erred in making the following findings of fact:

- (a) Paragraph XIX.
- (b) Paragraph XXI.
- (c) Paragraph XXII.
- (d) Paragraph XXIII.
- (e) Paragraph XXIV.
- (f) Paragraph XXV.
- (g) Paragraph XXVI.
- (h) That portion of Paragraph XXVII, as follows:

“and that in itself would be a construction contrary to the purpose of the contract and contrary to plaintiff’s avowed purpose at the time the contract was executed.”

(i) That portion of Paragraph XXVIII, as follows:

and in that contemplation the parties inserted in the contract the following provision:

‘Should a smelter or other reduction works be erected between the mining property herein conveyed and Cascade, Idaho, then there shall be deducted from the net smelter or reduction returns a fair charge for trucking from the mine to such smelter or reduction works.’

- (j) Paragraph XXIX.
- (k) Paragraph XXXI.
- (l) Paragraph XXXIII.

- (m) Paragraph XXXIV.
- (n) Paragraph XXXV.
- (o) Paragraph XXXVI.
- (p) Paragraph XXXVII.
- (q) Paragraph XXXVIII.
- (r) Paragraph XXXIX.
- (s) Paragraph XL.
- (t) Paragraph XLI.

II. The Court erred in concluding:

(a) Under paragraph II of its conclusions of law that the proper and legal method for determining the amount of royalty due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941 for minerals, ores, metals and values extracted from the mining claims described therein and smelted at the Yellow Pine Smelter of the defendant is by the use of "net smelter returns" provision as defined in the contract and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of salable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by the defendant at the Yellow Pine Smelter.

(b) Under paragraph III of its conclusions of law that the defendant does not owe plaintiff anything by way of royalties, or otherwise, for or on account of any ores, concentrates, metals or values taken from the mining claims described in said contract and processed at the Yellow Pine Smelter.

III. The Court erred in adjudging:

(a) In Paragraph I. of its Judgment, that the proper and legal method for determining the amount of royalties due the plaintiff under "Conveyance, Royalty Agreement and Option" dated December 31, 1941 for minerals, ores, metals or values extracted from the mining claims described thereon and smelted at the Yellow Pine Smelter of the defendant is by the use of "net smelter returns" provision as defined in the contract and that the plaintiff is not entitled to any royalty computed on the basis of the amount paid to the defendant by purchasers of salable products resulting from the smelting and reduction of minerals, ores, metals and values taken from said mining claims and smelted by defendant at the Yellow Pine Smelter.

(b) In Paragraph II. of its Judgment, that the defendant is not indebted to the plaintiff, and that the plaintiff is not entitled to recover from the defendant any monies by way of royalty, or otherwise, for and on account of any ores, concentrates, metals or values taken from the mining claims described in said "Conveyance, Royalty Agreement and Option" and processed at Yellow Pine Smelter.

STATEMENT OF ISSUES

The trial court erred in finding that the net smelter returns provisions of the contract of December 31, 1941, are applicable to the operations of the Yellow Pine Smelter (R. 45); and entering judgment in

accordance therewith (R. 65). The trial court erred in not finding that the net revenue clause of said contract is applicable to the operations of the Yellow Pine Smelter and in not entering judgment in conformity with such a finding.

ARGUMENT

First, let us look at the decisions of the court of May 15, 1956 wherein this court said:

“The ‘net smelter returns’ clause referred to by the District Court provides: ‘[Bradley shall] pay United . . . a royalty of five per cent (5%) on all net smelter returns. . . By net smelter returns, as used herein, is meant the amount received from the smelter from any and all ores, concentrates, metals or values shipped to a smelter, it being understood that the smelter will deduct its normal smelting charges. . . By its terms this clause is limited to situations where ‘amounts are received [by Bradley] from outside smelters.’ ”

“We see no reason why, as a matter of law, the ‘net revenue’ clause could not be controlling.’ ”

It is United’s position that the foregoing states the law of this case with reference to the meaning of the ‘net smelter returns’ clause in the contract. This clause has been eliminated from consideration by the lower court because it is limited to situations

where amounts are received by Bradley from outside smelters, and the evidence is uncontradicted that Bradley never received any money from any outside smelter for the concentrates processed at its Yellow Pine Smelter and which originated from the mining claims solely owned by Bradley.

The evidence adduced by the defendant at the trial was aimed at only one purpose, namely, to insist that the "net smelter returns" clause of the contract was applicable to the operations at the Yellow Pine Smelter, regardless of the law of the case and its own admissions that it never received any amount from outside smelters for the portion of the concentrates from the mining claims processed at the Yellow Pine Smelter.

There was no attempt on the part of Bradley to show that the "net revenue" clause of the contract did not apply or could not apply, other than its insistence that the "net smelter returns" clause did apply.

The trial court followed Bradley's contentions, disregarding the opinion of this court dated May 15, 1956.

United's objections to certain findings and conclusions (R. 448) are based on the ground, among others, that so far as they attempt to sustain the "net smelter returns" clause they are irrelevant and immaterial in view of this court's decision of May 15, 1956.

The evidence submitted by Bradley at the trial of this cause, presented no matters which were not before this court at the time of its opinion of May 15,

1956. Bradley's evidence at the trial was before this court previously in the affidavits and pleadings, interrogatories and answers, requests for admissions and admissions, when it decided previous appeal No. 14705 by its decision of May 15, 1956.

At the trial Bradley presented no new questions that were not before the court previously presented no evidence to show that certain subjects of negotiation which were intended to be covered by the new contract were not in fact so covered; no evidence that either party to the contract of December 31, 1941, had to go outside of the document itself to determine if the individual fact was covered; no evidence that there were any particular elements or extrinsic facts or negotiations which were not dealt with in the contract.

In fact, all of the matters adduced by Bradley at the trial were mentioned, covered and dealt with in the contract itself. The contract of December 31, 1941, represents a total meeting of the minds of the parties thereto respecting all matters therein contained. And the contract contains their agreed definition of the terms "net revenue" and "net smelter returns" which are clear, plain and unambiguous. In fact, Bradley does not claim that the terms are uncertain, unintelligible or ambiguous.

The contract of December 31, 1941, is unique. It is entirely separate, distinct and apart from the usual lease or lease and option agreement known to the mining industry. There is no evidence of any other contract of this kind or the constructions of any other

contract of this kind. It stands out clear and plain that Bradley acquired all of the mining claims and the values therein in consideration of the payments of certain sums of money computed simply by taking a certain percentage of amounts received from the sale of values extracted from the mining claims to an outside smelter or a United States mint or a purchaser, regardless of the state of concentration or refinement.

It is immaterial under the precise terms of the contract whether smelting is classified in the industry as a part of mining or as a step beyond mining, for the simple reason that Bradley owns the values, regardless of the state of refinement, and has agreed to pay a royalty on the basis of money received from a sale thereof, to an outside smelter, a mint or a purchaser.

This court, in remanding this cause, ruled on the law of the case:

Accordingly, there is no different question arising on this appeal nor does the record present a different state of facts and thus the determination of this court of May 15, 1956 was controlling on the lower court and is controlling in this appeal. The essential facts and evidence, issues and pleadings on the subsequent appeal are exactly similar on this appeal and the record presents no materially different situation and the doctrine of the law of the case thus has application to the former decision and this appeal and is not affected because there are no altered circumstances and there must be more than merely cumulative evi-

dence or immaterial evidence.

5 C.J.S., page 1288, Sec. 1834. *Bodkin vs. Edwards*, 9th Circuit Court of Appeals, 265 F. 621. Affirmed 41 S. Ct. 268, 255 U.S. 221, 65 L. Ed. 595.

In the case of *Bodkin vs. Edwards*, *supra*, it is stated:

“It is a rule of law, no longer to be controverted in the circuit courts, that whatever has been decided upon on one appeal cannot be re-examined in a subsequent appeal of the same suit or action. Thus far, the determination upon the first appeal becomes the law of the case and *res judicata*, and henceforth cannot again be questioned in the same case by the same parties to the suit or their privies . . . * * *

“Apply the rule here and seeing that the subsequent proceedings present no additional questions material to the issues, the former opinion of this court is decisive of the case upon appeal.”

The record fails to disclose any reason why the net revenue clause of the contract as a matter of law is not controlling.

In conclusion United contends that this court, in its former holding of May 15, 1956, ruled out any applicability of the “net smelter returns” clause to the operations of the Yellow Pine Smelter and urges that the lower court erred in finding to which exception has been taken, and particularly in finding that

the “net smelter returns” provisions apply to this case, and in so concluding and entering its judgment to that effect.

Respectfully submitted,

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By _____
Attorneys for Appellant.

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No. 15,653
United States Court of Appeals
For the Ninth Circuit

HARRY T. VON EICHELBERGER and HAIG
MIHRAM TERZIAN,

Appellants,

VS.

UNITED STATES OF AMERICA,

Appellee.

On Appeal from the United States District Court for
the Northern District of California,
Southern Division.

APPELLANTS' REPLY BRIEF.

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No. 15,653

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APPELLANTS' REPLY BRIEF.

Simply stated, appellants contend that the transfer of possession of the machine guns here in issue which occurred in December, 1956, is a transfer outside the scope and meaning of Chapter 53, Title 26, U.S.C. If there was no taxable transfer, the penalties invoked by appellee pursuant to 26 U.S.C. 5851 and 5861 are inapplicable.

Appellee cites *Montgomery v. United States*, 146 F. 2d 142 and *Rayborn v. United States*, 345 F. 2d 368 for the proposition that it was the intent of Congress to tax any transfer of possession. *Montgomery v.*

United States, ante, 146 F. 2d 142 is clearly inapplicable. It is a pleading case on its face. Defendant appellant had pleaded guilty to two charges, one, the improper *possession* of a machine gun upon the transfer of which no tax was paid and the second charge, that of *receiving* such an illegally transferred weapon. Appellant moved to vacate one of the judgments. He claimed that there was but one indivisible culpable act so that his consecutive sentences of five years and five years on each count constituted double punishment. The Court of Appeals held otherwise. So likewise is *Rayborn v. United States*, ante, 345 F. 2d 368 an identity of offense and pleading case. Consequently it is inapplicable. From the opinions of the instant Court of Appeals it cannot be determined, how or in what manner the several appellants had obtained possession of weapons in question. Certainly from these cited cases, no broad congressional intent to tax the mere transfer of possession may be drawn, imputed or inferred.

Congress has the constitutional power to tax a transfer of possession of machine guns from one person to another, *Sonzinsky v. United States*, 300 U.S. 506, 57 S.Ct. 554, 81 L.ed 772, *United States v. Cumbee*, 84 F. Supp. 390 and *United States v. Adams*, 11 F. Supp. 216. However, from this it obviously does not follow that all transfers of machine guns are violative of the statutes, particularly if Congress employs restrictive methods of definition as to what is a taxable transfer.

That appellants have not violated the *literal terms* of the statute is apparent. To bring them within the

statutory purview, appellee belabors the obvious, namely racketeers, gunmen and desperadoes, in a patent effort to expand the scope of the statute beyond that which Congress intended.

The phrase "or otherwise dispose of" is said by appellee to bring within the statutory intendment any "physical transfer of firearms" (page 15, Brief for the Appellee) or any "passage of physical possession" (page 15, Brief for the Appellee).

The term or expression "dispose of" according to the text writer in 27 C.J.S. 345 is said to have "no technical signification" and to be "nomen generalissimum", *Phelps v. Harris*, 101 U.S. 370, 25 L.ed 155. When "otherwise disposed of", is coupled with, preceded by or associated with "sale" it applies only to those transactions in which there has been a transfer of title or absolute possession of the property, *Scott v. State*, 6 Ga. App. 332, 64 S.E. 1005 and *State v. Gorman*, 113 Kan. 740, 216 P. 290.

Phelps v. Harris, ante, 101 U.S. 370, 25 L.ed 155, is of interest because of the peculiar nature of the problem at hand. The construction of a will and codicil was in issue. The will gave the trustee power "to sell or exchange" property. The codicil gave the trustee power "to dispose of" the property. The trustee partitioned land within his control. The Court held the partition to be valid as being within the scope of "to dispose of". By dictum, however, the Court said that had the words "to dispose of" been placed in context with and adjacent to "sell" a restricted meaning would then be given.

“prosecution” and “disposition of” the action for the collection of the statutory penalties. By “disposition” was meant the “administrative proceedings to obtain forfeitures.” The Court held that prosecution and disposition were nearly identical and closely related functions to obtain the same results and that “disposition” meant to settle, adjust or *finally fix* or determine a matter.

The decisions of the several state courts are classifiable upon the basis of a division between civil and criminal proceedings. In the former, or civil proceedings, two lines of authority may be found. One line of authority exemplified by *Roe v. Burt*, 66 Okla. 193, 168 P. 405 holds that when “dispose of” is associated with “sell” or “sale” an expanded meaning is attached to “dispose of” on the theory that “sell” is a “lesser and included” means of disposition. “Disposition” or “to dispose of” is described as “to exercise *finally* one’s power to control over, to pass over into the control of someone else, as by selling, to *alienate*, to *part with*, to relinquish or to get rid of.”

Of similar import is *People v. Rathbun*, N.Y., 21 Wend. 509, 526-527, wherein the Court said “dispose of” was equal to and synonymous with “putting away”.

See also *Barnard v. Barnard*, 91 Ga. App. 502, 86 S.E. 2d 533, 536 wherein “dispose of” was held to mean “*to divest one’s self of all rights and interest in the thing.*” In “Barnard”, the defendant had mortgaged the property in issue. The Court said that this was not a disposition within the meaning

of an acknowledgment of indebtedness which ordered defendant to pay to plaintiff on a debt should defendant "sell, exchange or otherwise dispose of" the property. Likewise equating sales, alienation and disposition is *Bieg v. Shamel*, 129 C.A. 2d 700, 708, 277 P. 2d 842. This line of authority is comparable therefore to the federal cases herein discussed as personified by *Platt v. Union Pacific R. R. Co.*, ante (1878), 99 U.S. 48, 59, 25 L.ed 424, 427, *Phelps v. Harris*, 101 U.S. 370, 25 L.ed 155 and *Dayton Brass Casting Co. v. Gilligan*, ante, 267 F. 872, and equates "dispose of" with alienation.

The other line of authority in civil cases is exemplified by *Hawxhurst v. Rathgeb*, 119 C. 531. Citing California cases and cases from other jurisdictions, it was held therein that where a grant of power was made to another where language such as "sell, transfer, and release" was utilized, that no implied and lesser powers such as "to mortgage or otherwise dispose of the property" were granted. It is an example of strict interpretation.

As to criminal cases, the writer ascertained the existence of two lines of authority. What may be called the expanded interpretation or liberal rule is exemplified by *State v. Deisting*, 33 Minn. 102, 22 N.W. 442. Defendant was convicted of giving a drink of beer to a friend pursuant to the terms of a statute that said "No person shall sell, vend, deal in, or dispose of any spirituous (sic), . . . malt . . . liquor". The Court said "dispose of" was meant to include other forms of disposal than those indicated by the preceding

words in the ordinance. “*Ejusdem generis*” was not applied nor was “*noscitur a sociis*”. See also two Delaware cases, *State v. Handy*, 105 A. 426, and *State v. Rothman*, 105 A. 427.

The overwhelming majority of state court decisions in criminal appeals holds that where “dispose of” or “otherwise dispose of” are found in association with sale or sell, convey, gift or give away, “*noscitur a sociis*” requires that “dispose of” be limited in meaning to transactions comparable to the associated words, i.e., sale, conveyance or gift. The following cases and jurisdictions are but a representative segment: *State v. Julien*, 48 Iowa 445, 447, *State v. Nienaber*, 347 Mo. 541, 148 S.W. 2d 537, 539, *Bullene v. Smith*, 73 Mo. 151, 161, *Scott v. State* (Georgia), 64 S.E. 1005, *Stenson v. State*, 43 Ga. App. 582, 159 S.E. 777, 778, *Roberson v. State*, 3 Texas App. 502, *In re Carr*, 16 R.I. 645, 19 Atl. 146, *Roberson v. State*, 100 Ala. 37, 14 So. 554, *Wood v. Territory*, 1 Ore. 223, *Albrecht v. People*, 78 Ill. 510, *Cruse v. Aden*, 127 Ill. 231, 20 N.E. 73 and *State v. Standish*, 37 Kan. 642, 10 P. 66.

Whichever view of the law is taken, either the liberal expanded version which equates “dispose of” with “alienation” or the restricted, association version which results from application of *noscitur a sociis*, the conditional sales transaction here in issue fails to constitute an alienation or final dispossession as concerns appellant von Eichelberger. Title to the guns remains in him subject to divestment by the performance of a condition subsequent by appellant Terzian, the payment of the full purchase price. If we apply

Platt v. Union Pacific R. R. Co., ante or *Phelps v. Harris*, ante, both Supreme Court of the United States decisions, or if we apply the rule of the overwhelming majority of state decisions such as *Scott v. State* or *State v. Deisting* or *State v. Julien*, all ante, the transaction in which appellants engaged is outside the purview of 26 U.S.C. 5848(10), the section which defines transfer in terms of "sale . . . or otherwise dispose of".

In the instant case, there being neither "transfer of title" because such transfer was conditioned upon payment of the full purchase price nor "transfer of absolute possession of the property" because of the condition subsequent discussed above, the transaction here involved fails to come within the word "sale".

Parenthetically, counsel for appellee has incompletely quoted C.C. 1721.3. On page 14 of the Brief for the Appellee the writer states that a sale may be absolute or conditional. To be correct the words "contract of" ought to be inserted before "sale" so as to read "a contract of sale or sale may be absolute or conditional". When this is done the obviously executory nature of a conditional sales situation becomes clearly apparent.

The legal distinctions between a sale, a contract to sell and a conditional sales agreement are elementary and are made patent and obvious by the text writer in 55 C.J. 39 and 41. A contract of sale is said to be distinguished from a sale in that "a *contract to sell* is merely a *promise*, of an *executory nature*, and until it is executed gives merely a right of action for its

breach or specific performance, and does not pass the property in the goods or chattel, whereas a sale is in the nature of a *conveyance* or *transfer of title*". See *Perata v. C. I. R.*, C.C.A. 9, 89 F. 2d 550, 552, where this court through Circuit Judges Wilbur, Mathews and Haney reversed a decision of the Board of Tax Appeals wherein the Board had assessed a deficiency against a taxpayer who had failed to report certain sums received in accordance with the terms of a syndicate agreement for the purchase of shares in a corporation, citing as authority for its ruling the language herein quoted from *Corpus Juris*.

Circuit Judge Haney, the writer of the Court's opinion, held that the agreement was a contract of sale and executory rather than an executed sale in the year for which the deficiency was assessed, thereby rendering invalid the deficiency.

A further distinction is made between contracts of sale and conditional sales agreements. The text writer in 55 C. J. 41, citing cases, states that "an executory contract of sale is distinguished from a conditional sale in that an executory contract is *absolutely to sell* at a future time while a conditional (sales) contract is *conditionally to sell*; in the one case the *performance* of the contract is *suspended* and deferred to a future time; in the other (conditional sale) the very *existence and performance* of the contract depends on a *contingency*". Citing additional cases the identical language is repeated in 77 C.J.S. 579. See also 78 C.J.S. 255 wherein the term "conditional sales" is distinguished from "sale" and an executory "contract of sale".

“[O]r otherwise dispose of” has offered no assistance as a method or device whereby appellants are brought within the ambit of 26 U.S.C. 5848 (10) “to transfer or transferred”. The transaction in question, admittedly an executory one, is not within the plain meaning of the statute nor is the transaction impliedly with the statute, as has been developed herein. Under such circumstances, appellants’ ambiguous status is manifest. They ought not to be convicted.

In sum, while Sections 5811, 5814 and 5851 detail what the taxpayer must do to comply with the statutes, no person is liable to perform these respective duties unless he is a taxpayer. He becomes a taxpayer only if machine guns were “transferred” within the scope of the chapter. If there was no taxable transfer, within the definitions of the statute, there is no tax due and payable. If no tax is due and payable, appellants may not be punished for their failure to pay the tax or make reports or possess the guns in question.

Although belabored by appellee, appellants’ knowledge of the statute and its interpretation thus becomes meaningless. For the same reasons discussed above, likewise meaningless is appellant von Eichelberger’s financial impoverishment.

What possible intent could Congress have had by the inclusion of 26 U.S.C. 5846, the “incorporation by reference” section. The administrative regulations promulgated by Treasury provide for monthly returns and payments pursuant to the chapters on Re-

tailers Excise Taxes (monthly returns and payments, Reg. 51, Secs. 320.70 and 320.71), and Manufacturers Excise Taxes (monthly returns and payments, Reg. 46, 1940, Sec. 316.200).

Thus Treasury has always considered that where partial payments are made on account of contracts which involve conditional sales, the seller, upon whom the duty to pay the tax is imposed, is not required to report each transaction as it occurs or each payment as it is received. He may wait a time with safety or at least until January 31 of the next year before he need account for partial receipts obtained in December of the previous year. As to partial payments received in January, these need not be reported until February 28 of the year in question.

Applied to the instant factual situation, at worst, appellant von Eichelberger ought to have filed a January tax return on the \$25.00 which he received from appellant Terzian in December, 1956, had usual standards of reports, returns and payments been followed.

The "variable standards" argument developed in the opening brief is to appellee ingenious but unpersuasive. Perhaps it will cease to be unpersuasive when consideration is given to the material herein developed in appellants' briefs.

Brief examination will be made to the limitation of action Point III in both briefs. Appellants take the position that 26 U.S.C. 5851 in no wise purports to describe a continuing offense, and this is true even

though a statutory burden of persuasion is imposed upon a defendant to explain his possession to the trier of the fact. If appellee's argument were to prevail, one who retained possession of stolen government property could be prosecuted therefor even though he received such property ten years before. Compare *United States v. Mendoza*, D.C.N.D. Cal., 122 F. Supp. 367 with *Bowles v. United States*, 73 F. 2d 772, 775, certiorari denied, 294 U. S. 710. See also *United States v. Stony* (1869), 27 Fed. Cas. 16,282 regarding the time limits placed upon the government where defendant has been in continuous possession of property illegally smuggled into the United States.

In conclusion, it is respectfully submitted that appellants have amply demonstrated the inapplicability of the charging statutes to them. They further have demonstrated the capricious nature of those statutes. Under all of the circumstances their several convictions ought to be reversed.

Dated, San Francisco, California,
December 11, 1957.

GREGORY S. STOUT,
Attorney for Appellants.



No. 15,653

IN THE
United States Court of Appeals
For the Ninth Circuit

HARRY T. VON EICHELBERGER and HAIG MIHRAM TERZIAN, vs. UNITED STATES OF AMERICA,	}	<i>Appellants,</i> <i>Appellee.</i>
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APPELLANTS' OPENING BRIEF.

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IV.

Appellants assert personal and separate rights to the seized evidence. Appellant Terzian additionally asserts an interest in the property where the seizure occurred. They are "parties aggrieved" within the meaning of Rule 41,	
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No. 15,653

IN THE

**United States Court of Appeals
For the Ninth Circuit**

HARRY T. VON EICHELBERGER and HAIG MIHRAM TERZIAN,	} <i>Appellants,</i>

VS.

UNITED STATES OF AMERICA,	} <i>Appellee.</i>

APPELLANTS' OPENING BRIEF.

JURISDICTION.

Jurisdiction is invoked pursuant to Section 7804, 26 U.S.C., Section 3231, 18 U.S.C., Sections 1291 and 1294, 28 U.S.C., and Rules 18 and 37(a) of the Federal Rules of Criminal Procedure.

STATEMENT OF THE CASE.

Appellant Harry T. von Eichelberger was indicted for twenty-four violations of Chapter 53, Machine Guns, 26 U.S.C. Eight counts which involved eight separate military submachine guns, charged appellant with failure to pay the \$200.00 per weapon transfer

tax prescribed by Section 5811, 26 U.S.C. Eight additional counts alleged that appellant transferred the same eight weapons to co-appellant Haig Mihram Terzian without the use of the Treasury order form required by Section 5814, 26 U.S.C. Finally, appellant was charged with the receipt of these same eight weapons from sellers who failed to pay the \$200.00 transfer tax or use the required order forms in violation of Section 5851, 26 U.S.C.

Co-appellant, Haig Mihram Terzian, was charged in eight counts with the receipt of the same eight machine guns in violation of Section 5851, 26 U.S.C.

Three counts against Harry T. von Eichelberger and one count against Haig Mihram Terzian were dismissed by the trial judge during the government's case (T.R. 84, vol. 2).

Prior to trial, appellants made motions to dismiss and to return and suppress the evidence against them (T.R. 33-35, vol. 1), which motions were denied without prejudice (T.R. 27, vol. 1). These motions were renewed and were denied by the trial judge (T.R. 29, vol. 1).

On behalf of appellant Harry T. von Eichelberger and during trial, a motion was made for the dismissal of seven counts of the indictment upon the grounds that these counts were barred by the statute of limitations, Section 6531, 26 U.S.C., (T.R. 39, vol. 1). The Court denied this motion (T.R. 29, vol. 1).

After conviction, motions for new trial and in arrest of judgment were made by appellants (T.R. 39

and 40, vol. 1). These motions were denied (T.R. 30, vol. 1).

After a Court trial, appellant Harry T. von Eichelberger was convicted on twenty-one counts. He was sentenced to six months imprisonment on each count, all to run concurrently and was fined \$100.00 on each count, or a total fine of \$2,100.00.

Co-appellant Haig Mihram Terzian was convicted on seven counts, concurrently sentenced to six months imprisonment on each and fined \$100.00 on each count, or a total fine of \$700.00.

Timely appeal was made to this Court from the judgment of conviction (T.R. 42 and 43, vol. 1).

FACTS.

Appellant Harry T. von Eichelberger was formerly the proprietor of the Far West Hobby Shop, a retail store located on Clement Street in San Francisco. This establishment catered to sportsmen of all types and included a gun department. Among his personal hobbies was the collection of military firearms. Included in his assortment was a representative selection of modern and antique weapons (T.R. 97, vol. 2).

Mr. von Eichelberger purchased government exhibit 1 (U.S. model M-3, caliber .45, submachine gun), exhibit 2 (U.S. model, H & R Reising, caliber .45, submachine gun), exhibit 4 (U.S. model, Thompson submachine gun, .45 caliber) and exhibit 8 (German 9mm caliber submachine gun) from an Air Force

Captain in 1945 (T.R. 104, vol. 2). He paid the latter \$800.00 for this group (T.R. 105, vol. 2). Government's exhibit 5 (German submachine gun of 9mm caliber) was purchased in 1949 by him from a Navy Captain for \$75.00 (T.R. 105-107, vol. 2). The two remaining weapons, an Italian Beretta 9mm submachine gun and a Russian 7.62mm submachine gun were purchased in 1950 by appellant von Eichelberger for \$100.00 from a Navy Lieutenant Commander. All of these weapons were sold by von Eichelberger to Terzian on December 5, 1956 (T.R. 97, vol. 2). A form of conditional sales contract whereby possession of the guns was given to Terzian, but von Eichelberger retained their title until the payment of the purchase price of \$300.00 was prepared by von Eichelberger and signed by appellants (T.R. 98, vol. 2). Terzian gave von Eichelberger three checks in part payment. The first check was for \$25.00 and was dated December 5, 1956. The other two checks, each for \$50.00, represent payments made in January, 1957 by Terzian pursuant to the tenor of the agreement. The agreement is defense exhibit "A" and the checks are "B" in evidence (T.R. 102 and 103, vol. 2).

As of February 14, 1957, Terzian owed von Eichelberger \$175.00. According to the contract, von Eichelberger was still owner of the several weapons here involved (T.R. 110, vol. 2).

To properly safeguard the weapons, about February 7, 1957, Terzian requested and was granted permission by his old friend Louis Trost to store them in Trost's garage in San Francisco (T.R. 17, vol. 2).

The submachine guns were boxed and stored (T.R. 15, vol. 2). Trost neither knew of the contents of the boxes nor had Terzian's permission to open the boxes for inspection (T.R. 17, 25 and 26, vol. 2).

On February 14, 1957 Trost went to the offices of the Bureau of Narcotic Enforcement in San Francisco and conversed with agents of the Bureau including John Trainor (T.R. 20-22, vol. 2). Agent Trainor and other went to Trost's garage and using screw drivers opened a group of boxes which contained the submachine guns (T.R. 22, 23, 36, vol. 2).

As between Trost and Terzian, for the storage of the boxes, no rent was charged. The apparent consideration was a favor in return for past favors (T.R. 28, vol. 2). Terzian was to be supplied with a key by Trost so he could enter at will (T.R. 29, vol. 2).

Of especial significance, and possibly determinative of the "search and seizure" issue herein developed, is Trost's answer to a question of him put by the prosecutor about his relationship with Terzian. The question and answer appear on page 31 of Volume 2 as follows:

"Q. Did you turn over possession of that garage to Mr. Terzian or did you merely let him store some articles in it?

A. I let him store, not only possession."

To view the evidence in a manner most favorable to appellee's position, the record supports the ultimate fact that agent Trainor had Trost's permission to enter his garage (T.R. 21, 22 and 39, vol. 2). On the

other hand, the record supports appellants' position that neither Terzian nor von Eichelberger gave permission to Trost or to the government agents to enter the garage, open the boxes and seize these weapons (T.R. 28, 40 and 110, vol. 2). Inasmuch as there was no search warrant (so stipulated by the government, T.R. 28, vol. 2), one of the principal issues for this Court's determination will be the validity of the search and seizure.

As will be developed, appellants assert personal interest in the property seized, either ownership or right to possession. In the absence of a "pressing emergency" or legal process including a search warrant, appellants contend that the search and seizure violates their constitutional rights and was unreasonable. Further, they contend that their motions to suppress ought to have been granted and that their convictions are not supported by legally admissible or sufficient evidence.

Prior to trial a written stipulation was entered into between the parties. Its purport is to admit that the weapons here involved are within the purview of Section 5848(a), 26 U.S.C. The stipulation further admits that no \$200.00 transfer tax was paid as required by Section 5811, 26 U.S.C., and that no order form was used by appellants as required by Section 5814, 26 U.S.C. The stipulation was read into the record of the trial (T.R. 32a and 33, vol. 2).

ISSUES.

Under several headings, appellants propose to demonstrate that their convictions ought to be reversed. We will show:

First. That the transfer of possession of the weapons on December 5, 1956, pursuant to the conditional sales contract of that date was not a "transfer" within the meaning of Chapter 53, Section 5848, 26 U.S.C. This follows because there was no sale, assignment, pledge, lease, loan, gift or final disposition of the weapons as between the parties that occurred on December 5, 1956. Therefore, the evidence to sustain appellants' convictions is legally insufficient.

Second. Chapter 53, which includes within it several provisions, Section 5846, is not complete and it is not self-executory. Other excise tax definitions and procedures are incorporated. Regulations must be promulgated by Treasury officials. Upon its face, the chapter is a trap for the unwary and unknowing, is ambiguous and uncertain, and so far as appellants are concerned violates procedural due process.

Third. The evidence conclusively shows that appellant von Eichelberger obtained possession of the weapons at times more than six years prior to commencement of this prosecution against him. Section 6531, 26 U.S.C., which provides for a six year limitation period, bars his conviction upon seven counts.

Fourth. Appellants assert personal and separate rights to the seized evidence. Appellant Terzian additionally asserts an interest in the garage where the

seizure occurred. They are "parties aggrieved" within the meaning of Rule 41, Federal Rules of Criminal Procedure. They assert their personal constitutional right to be protected against this unreasonable search and seizure. Since neither Trost nor the agents had appellants' permission to enter, open that which was secured and seize, they contend that the search was unreasonable so that their convictions are supported only by legally inadmissible evidence.

ARGUMENT AND AUTHORITIES.

I.

ON DECEMBER 5, 1956, APPELLANT VON EICHELBERGER TRANSFERRED POSSESSION OF THE WEAPONS TO APPELLANT TERZIAN PURSUANT TO A CONDITIONAL SALES CONTRACT. THERE WAS NO TRANSFER WITHIN THE MEANING OF THE SECTION WHICH DEFINES "TRANSFER". THUS THE CHARGING STATUTES ARE INAPPLICABLE, THE EVIDENCE TO SUSTAIN THE CONVICTIONS INSUFFICIENT AND APPELLANTS' CONVICTIONS ARE UNLAWFUL.

Chapter 53, 26 U.S.C. applies. The gist of the chapter as it pertains to the present factual situation is as follows:

1. A \$200.00 per weapon transfer tax is to be paid by the transferor [Section 5811 (a) and (b)].

2. A taxable transfer occurs upon a sale, an assignment, a pledge agreement, a lease, a loan, a gift [Section 5848 (10)]. Another classification of taxable transfers may occur if it is of a type

which falls within the provision of the statute which says "or otherwise dispose of".

3. The payment of the tax is represented by stamps [Section 5811 (c) (1)] affixed to an order form signed by transferee [Section 5814 (a) (c) (1)].

At the outset, the problem is to determine how the several words in Section 5848 (10) "Definitions" are to be interpreted. Since the section fails to define what is a "sale", a "loan" or any of the other included words, to what body of law do we turn for their definition?

Congress has plenary tax powers, *Burnet v. Harmel*, (1932), 287 U.S. 103, 110, 77 L.Ed. 199, 204, 53 S.Ct. 74. In the absence of statutory definition, nationwide uniformity demands that State law apply only where such application is the express or implied intent of Congress, *Weiss v. Weiner*, 279 U.S. 337, 73 L.Ed. 721, 49 S.Ct. 337. Since Congress failed to set up its own definitive criteria, California personal property law defining the involved legal interests applies, *Watson v. C.I.R.*, (1952), 345 U.S. 544, 97 L.Ed. 1232, 73 S.Ct. 848 and *Burnet v. Harmel*, ante, 287 U.S. 103, 77 L.Ed. 199, 53 S.Ct. 74.

No tax was paid, no order form was used, and the statutes apply to the guns in question. But is a "conditional sale" agreement a "sale"?

Before discussion of these issues, disposition of the other statutory words contained in Section 5848 (10) will be made, their legal connotations will be ex-

amined and a determination will be made if possibly they may fit this factual situation.

“Assign” or assignment in its broadest possible sense signifies any conveyance or transfer of either real or personal property, *Commercial Discount Co. v. Cowen*, 18 C. 2d 610, 614, 116 P. 2d 599. By normal usage, the word usually applies to the transfer of title to a *chose in action* from one person to another. Nowhere in 26 U.S.C. is “assign” or any of its variants defined. Since tangible personal property is here involved, it follows that this transfer between Harry T. von Eichelberger and Haig Mihram Terzian is not an assignment within the meaning of Section 5848 (10), 26 U.S.C.

Consideration will now be given to the meaning of the word “pledge” as it appears in Section 5848 (10), 26 U.S.C. Nowhere in 26 U.S.C., is this word defined. Under California law a pledge is defined as a deposit of personal property to secure performance of another act by the depositors, California Civil Code, Section 2986. This definition is likewise the common law meaning, 72 C.J.S., Pledges, Section 1, page 3 and *Nelson v. C.I.R.*, C.C.A. 8, 101 F. 2d 568. The instant factual situation does not fall within the scope of this word as set forth in Section 5848 (10), 26 U.S.C. as Harry T. von Eichelberger was under no further contractual obligation.

“Lease” as included in “transfer” is likewise undescribed. As applied to real property its meaning is clearly defined a common law and by statutory enactment as a document whereby a less than free-

hold estate is conveyed by one person to another, 51 C.J.S., Landlord and Tenant, Section 202, page 803, California Civil Code, Section 1624. Applied to the law of personalty, it has much the same connotation as a transaction in realty although the application of the term to a transaction in personalty is a misnomer. From the facts as herein narrated, no lease in the sub-machine guns was created as between appellants in as much as conditional possession of the weapons passed to Haig Mihram Terzian.

According to Section 5848 (10), 26 U.S.C., "transfer" includes "loan" and possibly its variant "to lend". Congress has not seen fit to define the term in the Internal Revenue Code, 26 U.S.C. However, California Civil Code, Section 1884, defines a loan as a contract for the temporary use of personalty. This is likewise its common law meaning, 54 C.J.C., Loan, page 653, and *Lancaster v. Jordan Auto Co.*, C.C.A. Miss., 121 F. 2d 912. As concerns appellants' relationship there was no loan transaction.

Section 5848 (10), 26 U.S.C., includes "give away" within the meaning of "transfer". Inferentially, its variant "gift" is included. Even in Chapter 12, Gift Tax, 26 U.S.C., the meaning of gift is undefined. California Civil Code, Section 1146 in effect states that a gift is a voluntary transfer of personal property without consideration. This is the common law definition, 38 C.J.S., Gifts, Section 1. a., page 799 and *Detroit Edison Co. v. C.I.R.*, 131 F. 2d 619. In the transfer between appellants there was consideration. Thus it would appear that the words "give away" as they

are found in Section 5848 (10), 26 U.S.C., are inapplicable.

Consideration will now be directed to the word "sell" as that word appears in Section 5848 (10), 26 U.S.C. Inasmuch as "sale" is a recognized variant, the common law as well as statutory definitions of "sale" must be scrutinized. No definition of either word is found in 26 U.S.C. In the absence of such definitions in the Internal Revenue Code, the several state definitions prevail. The Uniform Sales Act, enacted by the majority of the several States (at last count 38) distinguishes between sales and contracts to sell in its first section. In part, Section One of the Uniform Act or California Civil Code, Section 1721 is as follows:

"Contracts to sell and sales. (1) A contract to sell goods is a contract whereby the seller agrees to transfer the property in goods to the buyer for a consideration called the price. (2) A *sale* of goods is an agreement whereby the seller *transfers the property* in goods to the buyer for a consideration called the price. (3) A *contract to sell* or a sale may be *absolute* or *conditional* . . ." (Emphasis added.)

The distinction noted above is further emphasized by Section 3 of the Act, or California Civil Code, Section 1723. This section reads as follows:

"Form of contract for sale. Subject of the provisions of this act and of any statute in that behalf, a contract to sell or a sale may be made in writing (either with or without seal), or by word of mouth, or partly in writing and partly

by word of mouth, or may be inferred from the conduct of the parties.”

See California Civil Code, Section 1740(1) which recognizes that contracts of sale may be conditional in that possession of goods may be retained by the seller subject to performance by the buyer of certain conditions. While not a conditional sales agreement, it is comparable in its legal effectiveness.

See also, Section 2980, California Civil Code, which concerns recordation of certain types of conditional sales contracts and Sections 2981 and 2982, California Civil Code, as those sections apply to automobile conditional sales. California Civil Code, Section 2981, (a) (1) and (a) (2) define two generally acceptable forms of conditional sales agreements pertaining to auto sales. However, these definitions are also accepted where any type of personalty may be sold subject to a contract wherein the seller retains legal title subject to conditions subsequent to be performed by the buyer, 78 C.J.S., Sales, pages 254 and 255, 22 Cal. Jur., Sales, Section 146, pages 1095 and 1096, *Woodbine v. Van Horn*, 29 C. 2d 95, 173 P. 2d 17 (holding that in a writing the use of the words “sell, sold and convey” usually indicate that the contract is one of sale and absolute as distinguished from conditional.)

See also *Fine v. Bradshaw*, 138 C.A. 2d 862, 292 P. 2d 537 and *Lunny v. Labrucherie*, 103 C.A. 2d 865, 230 P. 2d 427 for what constitute a valid conditional sales contract and holding also that such transactions are

executory as distinguished from sales which are executed and absolute.

Two recent Supreme Court of the United States decisions discuss "sale" as the word is found in the chapter on personal income tax. One is *Helvering v. Hammel* (1940), 311 U.S. 504, 85 L.Ed. 303, 61 S.Ct. 368. The other is *Helvering v. William Flaccus Oak Leather Co.* (1940), 313 U.S. 247, 85 L.Ed. 1310, 61 S.Ct. 878. In the former case the Court held that a foreclosure sale of taxpayers' property was a capital loss. The Court through Mr. Justice Stone on page 507 of the official reporter discusses the meaning of "sale" and also applies some rules of statutory construction. In the latter case, the Court held that insurance money received from the destruction of a building by fire was ordinary income and not capital gain or loss income resulting from an involuntary sale or exchange of a capital asset.

The words "to transfer" and "transferred" in Section 5848 (10), 26 U.S.C., "include" the various types of transactions which previously have been discussed. Consideration now will be given to the legal meaning of "to transfer", "transferred" and their noun variant "transfer". The text writer in 87 C.J.S. Transfer, at pages 894 and 895 states as follows:

"As a verb. With certain exceptions, it is said that the verb cannot be held to have a well-defined technical legal meaning, and it is sometimes defined as meaning to bear over from one place to another, to carry across; and such meanings are often intended by its use. The verb 'transfer' is further defined as meaning to pass over; to con-

vey or pass over the right of one person in property to another; to convey as a right from one person to another, to convey or remove from one place, person, etc., to another; to make over the possession or control of; to place in the hands of another, to grant; to assign; to sell or give."

In California, transfer is defined as an act whereby *title* to property is *conveyed* from one living person to another, California Civil Code, Section 1039. According to *Commercial Discount Co. v. Cowen*, ante, 18 C. 2d 610, 116 P. 2d 599 "transfer" connotes the passage of title to property from one person to another. Thus, there has been a common law and statutory distinction drawn between a transfer and a sale on the one hand and a conditional, executory title retaining conditional sales contract on the other hand.

As used in Section 5848 (10), 26 U.S.C., the expression "or otherwise dispose of" must now be considered.

It is axiomatic that the Internal Revenue Code of 1954, 26 U.S.C., being both a penal and a tax statute, should be strictly construed against appellee, the government, and liberally construed in favor of the taxpayer, appellants herein, *United States v. Giles*, 300 U.S. 41, 81 L.Ed. 493, 57 S.Ct. 340; *United States v. Resnick*, 299 U.S. 207, 81 L.Ed. 127, 57 S.Ct. 126; *Porter v. C.I.R.*, 288 U.S. 436, 77 L.Ed. 880, 53 S.Ct. 451.

Where statutory ambiguities arise and doubtful application of a tax measure to the taxpayer ensues, such doubtful application is resolved in favor of the

taxpayer and against the government, *Hassett v. Welch*, 303 U.S. 303, 82 L.Ed. 858, 58 S.Ct. 559 and *Hevering v. Marshall*, same citation.

Usually the language of a revenue law is to be given its ordinary meaning, *Helvering v. William Flaccus Oak Leather Co.*, ante, 313 U.S. 247, 85 L.Ed. 1310, 61 S.Ct. 878, and *Helvering v. Hammel*, ante, 311 U.S. 504, 85 L.Ed. 303, 61 S.Ct. 368.

The maxim of statutory construction “*expressio unius est exclusio alterius*”, translated means “the mention of one is the exclusion of another”, “*expressum facit cessare tacitum*”, translated means “that which is expressed makes that which is implied to cease” and “*noscitur a sociis*” translated means “the meaning of doubtful words may be determined by reference to the associated words” apply, *United States v. Barnes*, 222 U.S. 513, 56 L.Ed. 291, 32 S.Ct. 117 and *Helvering v. Hammel*, ante, 311 U.S. 247, 85 L.Ed. 303, 61 S.Ct. 368.

If these rules are utilized in favor of appellants, an executory conditional sales agreement is a distinct and separate legal entity from a sale. Congress included such conditional sales agreements in other chapters of 26 U.S.C., [Retailers Excise Tax, Section 4053 (2) (3), 26 U.S.C.; Manufacturers Excise Tax, Section 4216 (c) (2) (3), 26 U.S.C.; Capital Stock Tax, Section 4351 (b), 26 U.S.C.; and Silver Bullion Tax, Section 4892, 26 U.S.C.].

The distinction between executory contracts of sale on the one hand and executed sales on the other hand

is borne out by other excise tax chapters. The “Definitions” Section 4761, 26 U.S.C., Marijuana, subdivision (4) “Transfer or transferred” provides as follows:

“The term ‘transfer’ or ‘transferred’ means any type of disposition resulting in a *change of possession*, but shall not include a transfer to a common carrier for the purpose of transporting marihuana.” (Emphasis.)

“(C)hange of possession” is the key phrase. Obviously, the Congress designedly used words of maximum application and scope by this language so that any change of possession of marijuana would be a taxable act.

If we consider Section 4892, 26 U.S.C., a similar analysis is possible. The chapter in which the section is found provides for a tax upon the “transfer” of silver bullion. Section 4892,—Definitions—(2) “Transfer” is as follows:

“The term ‘transfer’ means a *sale, agreement of sale, agreement to sell*, memorandum of sale or delivery of, or transfer, whether made by assignment in blank or by any delivery, or by any paper or agreement or memorandum or any other evidence of transfer or sale; or means to make a transfer as so defined.” (Emphasis.)

Inasmuch as the execution of an “agreement of sale” and “agreement to sell” are contracts which give rise to a taxable act, the execution of a conditional sales agreement, as defined in Section 1721,

California Civil Code (Section 1, Uniform Sales Act), would be within the purview of Section 4892.

Where identical expressions "transfer" or "transferred" are found in other excise statutes, but there are given a broader meaning than that expressed in Section 5848 (10), 26 U.S.C., it is inferred that Congress understood the legal meaning of the words and phrases that Congress employed and intended that varying meanings attach, *Atlantic Cleaners & Dyers v. United States*, 286 U.S. 427, 76 L.Ed. 1204, 52 S.Ct. 607.

All that Congress need have done to make the \$200.00 tax provided for in Section 5811, 26 U.S.C., applicable to the execution of a conditional sales agreement as here employed by appellants would have been to enact a definition section comparable either to the language of Section 4761 (4) or 4892 (2), 26 U.S.C.

Since there are no other words in Section 5848 (10), 26 U.S.C., that apply, the section ought not to be expanded beyond its plain context, *McBoyle v. United States*, 283 U.S. 25, 75 L.Ed. 861, 51 S.Ct. 340 (aeroplane not included within National Motor Vehicle Theft Act) and *Fasulo v. United States*, 272 U.S. 620, 71 L.Ed. 443, 47 S.Ct. 200 (mailing threatening letters is not within purview of statute which punishes obtaining money by fraud).

Applied to the factual situation here at hand, it is apparent that the statutes under which appellants were convicted are not applicable and that therefore

the evidence is legally insufficient to sustain their several convictions.

II.

PURSUANT TO SECTION 5846, 26 U.S.C., OTHER EXCISE TAX DEFINITIONS AND PROCEDURES ARE INCORPORATED BY REFERENCE INTO CHAPTER 53. THE EFFECT OF THEIR INCORPORATION IS TO ADD OTHER MEANINGS TO SECTIONS 5811, 5814, 5848 (10) AND 5851, 26 U.S.C. AS APPLIED TO THESE APPELLANTS, PROCEDURAL DUE PROCESS IS VIOLATED.

Section 5846, 26 U.S.C., is as follows:

“Other laws applicable. All provisions of law (including those relating to special taxes, to the assessment, collection, remission, and refund of internal revenue taxes, to the engraving, issuance, sale, accountability, cancellation, and distribution of taxpaid stamps provided for in the internal revenue laws, and to penalties) applicable with respect to the taxes imposed by sections 4701 and 4721, and all other provisions of the internal revenue laws shall, insofar as not inconsistent with the provisions of this chapter, be inapplicable with respect to the taxes imposed by sections 5811 (a), 5821 (a) and 5801.”

The legal effect of this reference section is to incorporate into Chapter 53, 26 U.S.C., the provisions of other excise tax sections to the same extent as if they were set forth in detail in Chapter 53, *Engel v. Davenport*, 271 U.S. 33, 70 L.Ed. 813, 46 S.Ct. 410. Thus incorporated are Sections 4053 (2) (3) 26 U.S.C., Retailers Excise Tax (conditional sales agreements in-

cluded in transfer), Section 4216 (c) (2) (3) 26 U.S.C., Manufacturers Excise Tax (conditional sales agreements included in transfer), Sections 4341, 4343 and 4351 (b) 26 U.S.C., Capital Stock (beneficial interests taxed), Section 4761 (4), 26 U.S.C., Marijuana Tax Act (change of possession is taxable transfer) and Section 4892, 26 U.S.C., Silver Bullion Tax Act (conditional sales agreements taxable).

Section 5846 specifically incorporates Section 4701 and 4721, 26 U.S.C., a part of Chapter 39—Regulatory Taxes, subchapter A—Narcotic Drugs and Marijuana. By its language, a one-cent an ounce tax is imposed upon certain sales of drugs. Does this tax apply to machine guns in addition to the \$200.00 transfer tax imposed according to Section 5811, 26 U.S.C.?

Section 4721, 26 U.S.C., states that an occupational tax on sellers is to be paid on or before July 1st of each year. Is this tax in addition to the \$200.00 per weapon transfer tax set forth in Section 5811, 26 U.S.C.? Parenthetically, since no tax due date is mentioned in Chapter 53, 26 U.S.C., may appellants choose to await July 1, 1957, before paying the \$200.00 tax per gun or the one-cent per ounce tax described in Section 4701, 26 U.S.C., ante?

For purposes of argument, let us assume that Section 5846, 26 U.S.C., is to be applied as written. Let us assume further that Section 5848 (10) "transfer or transferred" includes a conditional sales agreement. What then follows? Section 4053, 26 U.S.C., Retailers Excise Tax, provides that a proportionate

amount of tax imposed upon retailers' sales will be paid by the sellers as monies are paid by the buyers to the sellers on account of conditional sales agreements. A similar provision is found in Section 4216 (c), 26 U.S.C., Manufacturers Excise Taxes. The problem now is—is Section 5811, 26 U.S.C., modified by sections 4053 and 4216 (c), 26 U.S.C.? No inconsistency in application appears on the face of these several sections.

If Sections 4053 and 4216 (c) are incorporated by reference into Section 5811, 26, U.S.C., along with Section 4721, the taxpayer has these perilous alternatives. (1) Must he pay \$200.00 per gun to the Treasury Department immediately upon the transfer of the weapon? (2) May he pay a proportionate amount of the \$200.00 dependent upon the seller's receipt of installment payments? (3) May the seller taxpayer wait until July 1st of the tax year before paying all or a proportionate amount of the tax then due?

The instant taxpayer is compelled to choose a course of conduct among several apparently given to him by Congress at his peril.

Constitutional law and particularly procedural due process require that on its face a criminal statute must be sufficiently definite as to the conduct it proscribes or denounces that an ordinarily intelligent person might know that what he did does fall within the statute's prohibitory ambit, *United States v. Harriss* (1953), 347 U.S. 612, 98 L. Ed. 989, 74 S. Ct. 808.

At page 617 of the opinion, Mr. Chief Justice Warren, speaking for the Court's majority, states the rule to be as follows:

"The constitutional requirement of definiteness is violated by a criminal statute that fails to give a person of ordinary intelligence fair notice that his contemplated conduct is forbidden by the statute. The underlying principle is that no man shall be held criminally responsible for conduct which he could not reasonably understand to be proscribed."

See *United States v. Petrillo* (1947), 332 U.S. 1, 91 L. Ed. 1877, 67 S. Ct. 1538; *United States v. Cardiff* (1952), 344 U.S. 174, 97 L. Ed. 200, 73 S. Ct. 189. See also *Lanzetta v. New Jersey* (1939), 306 U.S. 451, 83 L. Ed. 888, 59 S. Ct. 618, where the Court's opinion as to the rule of certitude is quoted as follows:

"If on its face the challenged provision is repugnant to the due process clause, specification of details of the offense intended to be charged would not serve to validate it. . . . It is the statute, not the accusation under it, that prescribes the rule to govern conduct and warns against transgression. . . . No one may be required at peril of life, liberty or property to speculate as to the meaning of penal statutes. All are entitled to be informed as to what the State commands or forbids."

In conclusion, it appears from the face of the statutes themselves, Sections 5811, 5814, 5846, 5848 (10) and 5851 that they are sufficiently uncertain and ambiguous as to require the taxpayer to chart his

course of action at his peril. By so doing, due process is violated.

III.

THE EVIDENCE CONCLUSIVELY SHOWS THAT APPELLANT VON EICHELBERGER OBTAINED POSSESSION OF THE INSTANT SUBMACHINE GUNS AT TIMES MORE THAN SIX YEARS PRIOR TO THE COMMENCEMENT OF THIS PROSECUTION AGAINST HIM. SECTION 6531, 26 U.S.C., BARS HIS CONVICTION UPON SEVEN COUNTS.

Section 6531, 26 U.S.C., is as follows:

“No person shall be prosecuted, tried, or punished for any of the various offenses arising under the internal revenue laws unless the indictment is found or the information instituted within 3 years next after the commission of the offense, except that the period of limitation shall be 6 years . . .”

The evidence is uncontroverted that appellant von Eichelberger purchased these weapons in 1945, 1949 and 1950. All purchases occurred more than six years prior to 1957.

The language of Section 5851, 26 U.S.C., is as follows:

“Possessing firearms unlawfully transferred or made—It shall be unlawful for any person to receive or possess any firearm which has at any time been transferred in violation of sections 5811, 5812(b), 5813, 5814, 5844 or 5846, or which has at any time been made in violation of section 5821. Whenever on trial for violation of this section the defendant is shown to have or to have had possession of such firearm, such possession shall be

deemed sufficient evidence to authorize conviction, unless the defendant explains such possession to the satisfaction of the jury."

von Eichelberger contends that his penal liability arises when he (1) failed to pay the \$200.00 tax and/or (2) fails to use the prescribed order form. Further, he is of the opinion that the tax here imposed is an "act" not a "status" or "condition" tax.

It is the general rule that the statute of limitations begins to run in favor of a defendant from the moment that an indictment first could be filed.

This rule is enunciated in *United States v. Irvine* (1878), 98 U.S. 450, 25 L. Ed. 193. Mr. Justice Miller stated the rule to be as follows:

"Whenever the act or series of acts necessary to constitute a . . . crime is complete, and from that day on the Statute of Limitations begins to run against the prosecution."

Further, he says:

"There is in this but one offense. (The withholding of money by a lawyer from a client.) When it is committed, the party is guilty and is subject to criminal prosecution, and from that time, also, the Statute of Limitations applicable to the offense begins to run."

United States v. Irvine, ante, has been followed without deviation since its writing. In *United States v. Kissel*, 218 U.S. 601, 54 L. Ed. 1168, 31 S. Ct. 124, where the exception of a continuing conspiracy was

first enunciated, speaking for the Court, Mr. Justice Holmes states the general rule to be:

“... (M)ere continuance of the result of a crime does not continue the crime.”

United States v. Irvine, ante, and *United States v. Kissel*, ante, are followed without deviation but with the usual embellishments. The Supreme Court of the United States applied the rule enunciated in *Irvine* to the cases of *Pendergast v. United States*, 317 U.S. 412, 417-418, 87 L. Ed. 368, 372, 63 S. Ct. 268; *Fiswick v. United States*, 329 U.S. 211, 216-217, 91 L. Ed. 196, 200, 67 S. Ct. 224; *Marzani v. United States*, 335 U.S. 895, 93 L. Ed. 431, 69 S. Ct. 297, 168 F. 2d 133; and *Bridges v. United States*, 346 U.S. 209, 97 L. Ed. 1557, 73 S. Ct. 1055. See *Bramblett v. United States*, D. of C. Cir., 231 F. 2d 489; *Butzman v. United States*, 6 Cir., 205 F. 2d 343, 351; and *United States v. Mendoza*, D.C.N.D. Cal., 122 F. Supp. 367, 368. See also *Grunewald v. United States*, 1 L. Ed. 2d 931.

Applied to the factual situation here present, no act save that of continuous possession occurred during the period 1950 to 1957. The obligations and duties imposed upon von Eichelberger by Chapter 53, 26 U.S.C., Sections 5811, 5814 and 5851 required him to prepare an order form and pay a \$200.00 per gun transfer tax. His duties were fixed at that time. No provision in 26 U.S.C., requires him each day, each month, each year to perform these statutory duties. As a matter of fact the regulations prepared by the Commission of Internal Revenue to Sections 5811

and 5814 compel payment of the \$200.00 tax and preparation of the order form before possession of the guns may pass from seller to buyer. Thus, the violation of Section 5851 is fixed by the illegal transfer of the guns from seller to buyer without use of the order form and payment of the tax. From these days forward the statute of limitations ought to run in favor of appellant von Eichenberger.

IV.

APPELLANTS ASSERT PERSONAL AND SEPARATE RIGHTS TO THE SEIZED EVIDENCE. APPELLANT TERZIAN ADDITIONALLY ASSERTS AN INTEREST IN THE PROPERTY WHERE THE SEIZURE OCCURRED. THEY ARE "PARTIES AGGRIEVED" WITHIN THE MEANING OF RULE 41, FEDERAL RULES OF CRIMINAL PROCEDURE. THEY ASSERT THEIR CONSTITUTIONAL RIGHT TO BE PROTECTED AGAINST THIS UNREASONABLE SEARCH AND SEIZURE. SINCE NEITHER TROST NOR THE AGENTS HAD APPELLANTS' PERMISSION TO ENTER, OPEN THAT WHICH WAS SECURED AND SEIZED, THEY CONTEND THAT THE SEARCH WAS UNREASONABLE AND THE EVIDENCE LEGALLY INSUFFICIENT TO SUPPORT THEIR CONVICTIONS.

Appellant Harry T. von Eichelberger asserts ownership of the submachine guns here in issue pursuant to the provision of the conditional sales agreement of December 5, 1956. Appellant Haig Mihram Terzian claims that he had a right to the possession of those same weapons by the agreement. Further, Haig Mihram Terzian states that he had an interest in Louis Trost's garage at 80 Julien Avenue, San Francisco. This interest, under California law, is known as a license.

A license is created in real property when the landlord retains his use and occupation of the premises but gives to the licensee a right of joint use and occupancy, *Kaiser Co. v. Reid* (1947), 30 C. 2d 610, 184 P. 2d 879 and *Takahashi v. Fish and Game Commission* (1947), 30 C. 2d 719, 185 P. 2d 805.

Sections 282, 282a, 282b and 282c, 5 U.S.C., establish the Bureau of Narcotics. Sections 7601-7606, 26 U.S.C., authorize inspection of places where taxable goods may be found. Rule 41, Federal Rules of Criminal Procedure, the adoption of which is provided for in Section 3041, 18 U.S.C., requires a search warrant in order that an entry into private premises be lawful. An exception is noted, to-wit, section 2236, 18 U.S.C., which provides that a federal agent may lawfully enter premises if there is either consent or invitation to enter.

The government will contend that the entry of the agents in Trost's garage was by Trost's invitation and consent. This is not disputed. However, without authority from Terzian, Trost may not give permission to strangers to open secured boxes (no machine guns were in plain view, *Marron v. United States*, 275 U.S. 192, 72 L. Ed. 231, 48 S. Ct. 74).

Ownership of the property seized (appellant Harry T. von Eichelberger) or the right to possess the property seized (appellant Haig Mihram Terzian) plus an interest in the premises where the property was seized (appellant Haig Mihram Terzian) are sufficient legal interests upon which appellants may assert their con-

stitutional privilege against an unreasonable search and seizure as here conducted by United States agents without lawful process, *United States v. Jeffers*, 342 U.S. 48, 96 L. Ed. 59, 72 S. Ct. 93 and *Klee v. United States* (1931, C.C.A. 9), 53 F. 2d 58.

The evidence is legally insufficient to sustain their convictions without the evidence that was unreasonably procured.

CONCLUSION.

Appellants respectfully pray for the reversal of their several convictions, with direction to the trial Court to enter a judgment of acquittal on all counts.

Dated, San Francisco, California,
September 16, 1957.

Respectfully submitted,

GREGORY S. STOUT,

Attorney for Appellants.

No. 15,653

IN THE

United States Court of Appeals
For the Ninth Circuit

HARRY T. VON EICHELBERGER and
HAIG MIHRAM TERZIAN,
Appellants,

VS.

UNITED STATES OF AMERICA,
Appellee.

On Appeal from the United States District Court for
the Northern District of California,
Southern Division.

BRIEF FOR THE APPELLEE.

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No. 15,653

IN THE

**United States Court of Appeals
For the Ninth Circuit**

HARRY T. VON EICHELBERGER and

HAIG MIHRAM TERZIAN,

Appellants,

VS.

UNITED STATES OF AMERICA,

Appellee.

**On Appeal from the United States District Court for
the Northern District of California,
Southern Division.**

BRIEF FOR THE APPELLEE.

JURISDICTION.

On March 6, 1957 an indictment in thirty two counts was filed in the United States District Court for the Northern District of California, Southern Division, charging appellants with violations of Section 5861, Internal Revenue Code of 1954 (26 U.S.C. Sec. 5861). Appellant von Eichelberger was charged in counts one to eight with failure to pay the tax imposed by Section 5811 IRC (26 U.S.C. Sec. 5811) on transfers of

firearms; in counts 9 to 16 with transferring firearms not in pursuance of a written order as provided by Section 5814 IRC (26 U.S.C. Sec. 5814); and in counts 17 to 24 with possession of firearms which had been unlawfully transferred to him in violation of Section 5851 IRC (26 U.S.C. Sec. 5851).

Appellant Terzian was charged in counts 25 to 32 with possession of firearms which had been illegally transferred to him in violation of Section 5851, IRC (26 U.S.C. Sec. 5851) (Tr. 19-23, Vol. 1).

Appellants waived trial by jury and were tried on April 29 and 30, 1957 before Chief Judge Michael J. Roche and found guilty as charged to all counts, except as to counts 3, 11 and 19 which were dismissed as to appellant von Eichelberger and count 27 which was dismissed as to appellant Terzian (Tr. 24-26, Vol. 1, Tr. 84, Vol. 2).

Judgment was imposed on May 28, 1957 wherein appellant von Eichelberger was sentenced to imprisonment for six months and fined \$100 on each count for a total fine of \$2,100, and appellant Terzian was sentenced to imprisonment for six months and fined \$100 on each count for a total fine of \$700 (Tr. 24-26, Vol. 1).

Notice of appeal was timely filed on May 29, 1957 (Tr. 42-44, Vol. 1). Jurisdiction of this court is invoked under Title 28 United States Code, Sections 1291, 1294; Title 26 U.S.C. Sec. 7804; Title 18 U.S.C. Sec. 3231; and Rules 18 and 37(a), Federal Rules of Criminal Procedure.

STATEMENT OF THE CASE.

The indictment herein, in 32 counts, relates to eight submachine guns originally obtained by appellant von Eichelberger from various sources and sold by him to appellant Terzian on December 5, 1956. The first eight counts charge appellant von Eichelberger with transfer of the guns to appellant Terzian without payment of the \$200 transfer tax imposed by Section 5811, Internal Revenue Code; the second eight counts charge transfer of the guns without a written order as prescribed in Section 5814, Internal Revenue Code; the seventeenth to twenty-fourth counts charge appellant von Eichelberger with possession of the guns illegally transferred to him in violation of Section 5851, Internal Revenue Code; and the last eight counts charge appellant Terzian with possession of the guns illegally transferred to him by appellant von Eichelberger in violation of Section 5851, Internal Revenue Code. The penalty for all of the foregoing violations is contained in Section 5861, Internal Revenue Code.

The facts in the case are largely undisputed. Appellants stipulated that they were not importers, manufacturers or dealers in firearms; that the guns in question were firearms within the meaning of the statute¹; and that no order forms were submitted as required by Section 5814, Internal Revenue Code (Tr. 36-38, Vol. 1; Tr. 32-33A, Vol. 2).

¹Despite this stipulation, the court dismissed counts 3, 11, 19 and 27 upon a showing that the agents were unable to field test the weapon described in those counts for automatic firing (Tr. 76-84, Vol. 2).

Appellant von Eichelberger was formerly proprietor of the Far West Hobby Shop, dealing with firearms of all types, and also maintained a private collection of firearms. Both appellants were generally familiar with the statutes regulating dealings in guns, and appellant von Eichelberger had on various occasions acted as a consultant for the Treasury Department in matters relating to firearms. (Tr. 43-44; 47; 70-75; 93-97; 117-121; 128-129; 138, Vol. 2). Appellants had prior dealings in firearms between them going back over a period of eight years (Tr. 97, Vol. 2).

Appellant von Eichelberger sold a quantity of firearms, including the eight described in the indictment, to appellant Terzian for \$300 on December 5, 1956. (Tr. 97, 132-133, Vol. 2). The estimated market value of these guns was \$3000, and von Eichelberger admitted that he knew the transfer tax on the fifteen guns involved in the transaction would aggregate \$3000 and that he was responsible for the payment of this amount, but that he had no money to pay the tax. (Tr. 123-126, Vol. 2).

Both appellants knew the machine guns in question were subject to the provisions of the National Firearms Act and in violation of the statutes regulating the taxation, transfer, possession and registration of firearms (Tr. 50, 64, 70-75; 103, 115, Vol. 2).

Appellant Terzian took physical possession of the firearms on December 5, 1956, and the appellants testified that they entered into a "Conditional Sales Contract" on the same date (Tr. 98-102; 111-112;

131-133, Vol. 2). The so-called "Conditional Sales Contract" provides as follows (Def. Ex. A):

"This agreement made between Harry von Eichelberger and Haig Terzian this day of December 5th, 1956, as follows:

(1) Haig Terzian has bought from Harry von Eichelberger and Harry von Eichelberger has sold to Haig Terzian 14 machine guns and misc. parts.

(2) Haig Terzian agrees to pay Harry von Eichelberger \$300.00 for said guns and misc. parts; \$25.00 down; \$100.00 before January 15th 1957 and the balance before June 1, 1957.

(3) Title to said guns shall remain in Harry von Eichelberger's name until the full price of \$300.00 shall be paid. Possession only is transferred to Haig Terzian at this time.

In the event that Haig Terzian fails to pay the balance of the purchase price, Harry von Eichelberger shall have the right to regain possession of said guns and misc. parts."

Pursuant to this agreement, Terzian paid \$25.00 by check on December 5, 1956 and \$50 each on January 5 and 9, 1957 (Tr. 59-62; 98-99, Vol. 2, Ex. 10, Def. Ex. B).² The \$175 balance of the purchase price was not yet due and had not been paid at time of trial (Tr. 114-115; 132, Vol. 2).

In a signed statement given to agents of the Alcohol and Tobacco Tax Division on February 20, 1957, appellant von Eichelberger admitted the "sale" of the

²The checks in Exhibit B are dated January 5 and January 9, 1956, but it is conceded that both were drawn in 1957.

various guns and made no reference to a conditional sales agreement (Tr. 123, Vol. 2, Ex. 11).

In his first statement to the investigators on February 14, 1957 appellant Terzian asserted that he had bought the various guns singly or in twos or threes and specified the prices paid for the various guns. (Tr. 50-54, Vol. 2, Ex. 13). No reference was made to a conditional sales contract on that occasion. (Tr. 56, Vol. 2). However, in a later statement on February 18, 1957 appellant Terzian told Agent Howland that his previous statement was not correct, and changed his statement to conform to his trial testimony (Gov't Ex. 9, Tr. 56-59, Vol. 2). The principle change in the second statement was that he had bought the guns all at once for an agreed price of \$300 and had paid \$125 toward the purchase price (Tr. 58, Vol. 2).

On cross-examination appellant Terzian admitted that he was free to store the guns any place he wished (Tr. 134, Vol. 2). Appellant von Eichelberger admitted that he did not know what Terzian did with the guns once he had taken them home. (Tr. 114, Vol. 2).

In early February, 1957 (fixed as the 3rd or 4th day of the month by appellant Terzian) the firearms were taken by Terzian in a box or boxes, with one weapon wrapped in a blanket, to a garage on the premises at 80 Julian Street, San Francisco for storage (Tr. 16-17; 131-136, Vol. 2). The garage premises were in an apartment-rooming house where the witness Trost resided, and were in Trost's exclu-

sive possession. The only access to the garage was through a single door which was kept locked at all times, and to which only Trost had the key. (Tr. 13-19, Vol. 2). At Terzian's request, Trost permitted him to store the boxes of machine guns and the blanket-wrapped rifle in the garage. Trost knew a rifle was wrapped in the blanket, but he did not know what was in the boxes. (Tr. 15-18, Vol. 2). Trost told Terzian he would give him a key to the garage and he had one made for that purpose, but it was defective and was not delivered to Terzian (Tr. 18, Vol. 2). Trost used the garage for storage of various items connected with his parking lot business located across the street. (Tr. 18-19, Vol. 2).

Trost did not know appellant von Eichelberger (Tr. 14, Vol. 2) and von Eichelberger did not know of or arrange for the storage of the guns on Trost's premises (Tr. 113, Vol. 2).

Appellant Terzian admitted that he could enter the garage only with Trost's permission, and by use of Trost's key; that he did not live on the premises, and that he paid nothing for the use of the storage space (Tr. 132-136, Vol. 2).

About a week after the boxes had been stored in his garage, Trost observed Terzian's picture in the newspaper and thereupon called at the Bureau of Narcotics where he informed Agent Trainor of the circumstances of the storage of the boxes. Trost and three agents of the Bureau of Narcotics returned to the premises at 80 Julian Street where Trost unlocked the garage door and pointed out the boxes. The boxes

were opened then taken away with their contents by the Narcotics Agents (Tr. 21-25; 34-39, Vol. 2). The action of the Narcotic Agents was with the consent and cooperation of Trost. (Tr. 24, 39, Vol. 2).

On cross-examination Trost testified that he did not have Terzian's permission to open the boxes, and it was stipulated that no search warrant had been issued. (Tr. 25-29, Vol. 2).

Appellant von Eichelberger testified that he had acquired the four guns, being Exhibits 1, 2, 4 and 8, in 1945 while employed at the Far West Hobby Shop; that he purchased them for \$800 from an individual wearing an Air Force uniform, and representing himself to be the personal pilot for Prime Minister Winston Churchill; that he did not obtain an order blank from the seller; that no tax was paid on the transfer of the guns to him; and that he did not register the guns with the Alcohol and Tobacco Tax Division, although aware he was required to do so. (Tr. 104-105; 115, Vol. 2).

von Eichelberger further testified he obtained the machine gun in evidence as Exhibit 5 from a Navy Captain for \$75 about 1949 at San Francisco. (Tr. 105-108; 116, Vol. 2), and that Exhibits 6 and 7 were purchased for \$175.00 in 1950 from a Navy Lieutenant Commander who refused to give his name. (Tr. 108-110; 116-117, Vol. 2). He admitted that no order blank was made as required by Section 5814; no tax was paid on the transfer of the guns as required by Section 5811, and none of the guns were registered by him with the Alcohol and Tobacco Tax

Division, although he knew of these requirements of the law. (Tr. 115-120, Vol. 2).

STATUTES INVOLVED.

The statutes involved are set forth in the appendix.

QUESTIONS PRESENTED.

1. Whether the sale and delivery of firearms pursuant to a conditional sales contract constitutes a "transfer" within the meaning of the definition contained in Section 5848(10), Title 26, United States Code.

2. Whether Section 5846, Title 26, United States Code, incorporating other provisions of the Internal Revenue Code by reference, is applicable so as to alter, modify or amend provisions of the Internal Revenue Code regulating dealings in firearms.

3. Whether the statute of limitations has barred prosecution of appellant von Eichelberger on counts 17 to 24 of the indictment.

4. Whether the search of a garage with the consent of the legal occupant, and the seizure of contraband firearms stored therein by appellant Terzian, constitutes an unreasonable search and seizure in violation of appellant's rights under the Fourth Amendment.

SUMMARY OF ARGUMENT.**I.**

By including the words "or otherwise dispose of" in the definition of "transfer" as applied to dealings in firearms under Section 5848(10), Title 26, United States Code, Congress intended to regulate the physical transfer of firearms from one person to another, irrespective of the transfer of legal title. Accordingly, machine guns sold on a conditional sales contract and physically transferred from the seller to the buyer constitute transfers within the meaning of the statute. In addition, a conditional sale falls within the scope of the general term "to sell" as defined under "transfer" in the statute, and failure of Congress to include the term "conditional sale" under the definition of "transfer" does not indicate an intent to exempt such transfers from the operation of the statute.

II.

The statutes defining the duties of persons dealing in firearms, and setting forth penalties for violation of such duties, are clear and precise. The indictment herein charges violations of the pertinent sections of the Internal Revenue Code without reference to any matters incorporated by inference from other portions of the Code. Whatever else be the effect of Section 5846, Title 26, United States Code (in applying provisions of other internal revenue laws not inconsistent with those in Chapter 53 dealing with firearms), it clearly does not alter, amend or modify the duties and penalties for evasion of such duties

set forth unequivocally in the chapter dealing specifically with firearms. In any event, appellants have failed to allege or prove that they were in any way misled or confused as to the meaning of the statutes involved, but to the contrary have conceded that they were aware of the law and simply failed to follow its dictates.

III.

The gist of the offense charged in counts 17 to 24, inclusive, is the possession of firearms within the period of the statute of limitations. Section 5851, Title 26, United States Code makes it unlawful to possess a firearm which has at any time been transferred in violation of the provisions of Sections 5811 or 5814, Title 26, United States Code. Concededly, appellant von Eichelberger possessed within the period of the statute of limitations certain firearms unlawfully transferred to him. That he received these firearms unlawfully in 1950 and earlier does not bar his prosecution for possession during the period of the statute of limitations. In general, the statute of limitations does not apply when some portion of the crime is within the period, although another portion is not. To hold that the statute of limitations began to run upon the unlawful receipt of the weapons insofar as prosecution under Section 5851 is concerned, would permit a defendant to escape the requirements of the law by the mere expedient of concealing his wrongdoing for the period of the statute of limitations. That this was not the intent of Congress is shown by the language of the statute

prohibiting possession "at any time" of illegally transferred firearms.

IV.

The search of a garage in which appellants had no interest, and the seizure of contraband firearms with the consent and by the invitation of the legal occupant of the premises, did not violate the rights of either appellant under the Fourth Amendment. The evidence was not taken from appellants, but from a third party who voluntarily relinquished it. Moreover, the place searched was a garage and therefore not within the protection of the Fourth Amendment. Finally, the evidence seized was contraband and appellants have failed to show that they, or either of them, had sufficient interest in the premises searched or the property seized to complain of the seizure.

ARGUMENT.

I.

THE SALE AND DELIVERY OF FIREARMS BETWEEN APPELLANTS CONSTITUTES A "TRANSFER" OF MACHINE GUNS WITHIN THE MEANING OF THE STATUTE REGULATING SUCH TRANSFER.

Appellants' opening argument is that the sale and delivery of the firearms in question does not constitute a "transfer" as that term is defined in Section 5848(10), Title 26, United States Code, and that therefore they were not required to comply with the requirements of Section 5811 and 5814, Title 26, United States Code, regulating such transfers.

Section 5811(a), Title 26, United States Code imposes a tax of \$200 on firearms "transferred" in the United States; the tax to be paid by the transferor (subsection (b)); and to be represented by stamps (subsection (c)).

Section 5814(a), Title 26, United States Code makes it unlawful for any person to "transfer a firearm except in pursuance of a written order from the person seeking to obtain such article" on an order form issued in blank for such purpose by the Secretary [of the Treasury] or his delegate.

The term "transfer" is defined in Section 5848(10), Title 26, United States Code as follows:

"(10) To transfer or transferred.—The term 'to transfer' or 'transferred' shall include to sell, assign, pledge, lease, loan, give away, or otherwise dispose of."

It is appellant's contention that since the guns in question were transferred from appellant von Eichelberger to appellant Terzian pursuant to a so-called "conditional sales agreement," which method of transfer is not expressly included in the definition contained in Section 5848(10), such transfers are excluded from the operation of the statute.

Briefly, the facts show that appellants negotiated on December 5, 1956 for the sale of a quantity of machine guns and miscellaneous parts, including the eight guns described in the indictment; that appellant Terzian paid \$25.00 down and agreed to pay the balance of the \$300 purchase price in installments;

that appellant Terzian received physical custody and possession of the guns immediately upon the payment of the \$25.00, and that he retained exclusive custody of the guns thereafter.

The broad Congressional intent to prohibit the physical transfer of firearms except in accordance with the provisions of Chapter 53, Internal Revenue Code, is amply demonstrated by the use of the words "or otherwise dispose of" in the definition of the word transfer in Section 5848(10). The method of handling the machine guns adopted by appellants, whether or not falling within the technical legal definition of "sale," nevertheless constitutes a transfer from von Eichelberger to Terzian under the broad phrase "or otherwise dispose of." It would be a perversion of the congressional intent to permit appellants by use of legal semantics to avoid the logical and reasonable intendments of the statute.

Moreover, it is believed that the machine guns were transferred as sold within the meaning of the word "to sell" in Section 5848(10). Under California law, "A sale of goods is an agreement whereby the seller transfers the property in goods to the buyer for a consideration called the price." California Civil Code, Section 1721(2). "Sell" is not a word of fixed and invariable meaning, but may be given a narrow or broad meaning, according to the context or the surrounding circumstances. *W. F. Boardman Co. v. Petch*, 199 P. 1047, 186 C. 476. A sale may be conditional or absolute. (California Civil Code, Section 1721(3)) and will generally be given

a broader significance where the meaning of the law demands it. *Mansfield v. District Agr. Ass'n No. 6*, 97 P. 150, 154 C. 145.

It is clear that Congress intended to regulate the physical transfer of firearms, irrespective of whether legal title passed with the weapons or remained in the transferor. No other logical conclusion is possible in view of the definition of "transfer" in Section 5848(10). If it were intended that both possession and legal title must pass to complete a transfer, there would appear no valid reason for including assignments, pledges, leases, and loans of firearms as transfers, since in all such circumstances title remains in the assignor, pledgor, lessor or lender. The interpretation of the statute argued for by appellants would frustrate the Congressional motive to prevent racketeers, bank robbers and desperadoes from obtaining machine guns and other firearms, and to enable the federal government to trace the ownership of firearms. *United States v. Adams*, 11 F. Supp., 216 (D.C. Fla., 1935).

That passage of physical possession rather than legal title is the touchstone of the offense is further demonstrated by decisions of two circuits that possession of *stolen* guns, constitute offenses when they have not been properly transferred in compliance with the statutes here involved. *Montgomery v. United States*, 146 F. 2d 142 (C.A. 4th, 1944); *Rayborn v. United States*, 234 F. 2d 368 (C.A. 6th, 1956). Certainly if a theft of a firearm constitutes a taxable transfer within the meaning of the statute, the sale

of guns, whether conditional or absolute, and the physical transfer of possession from the transferor to the transferee falls within the scope of transfers intended to be regulated.

II.

THE STATUTES ARE CLEAR AND UNAMBIGUOUS IN DEFINING APPELLANTS' DUTIES AND IN PROVIDING PENALTIES FOR VIOLATIONS OF SUCH DUTIES.

Appellants suggest that Section 5846, Title 26, United States Code making applicable all provisions of law with respect to taxes on narcotic drugs, and all other provisions of the internal revenue laws "insofar as not inconsistent with the provisions of this Chapter" incorporates various other sections of the Internal Revenue Code to such a degree that the statute is not sufficiently definite to satisfy procedural due process (App. Br. 19-23).

Appellants' argument is ingenious but without merit. Section 5846 in no way alters, amends or modifies the requirements set forth in Chapter 53 of the Internal Revenue Code for dealing with firearms. Nor are appellants charged in the indictment with any offenses incorporated by reference from other chapters of the Internal Revenue Code. The indictment is a plain, concise and definite written statement of the offenses charged under Section 5861, Title 26, United States Code, and clearly alleges failure to comply with Section 5811 relating to payment of the transfer tax, Section 5814 relating to transfer pursu-

ant to a written order, and Section 5851 relating to possession of firearms unlawfully transferred.

In short, the statutes under which appellants are charged define specific duties and provide specific penalties for violation of such duties. There is no ambiguity in Sections 5811, 5814 or 5851 defining the duties and no doubt as to the penalties contained in Section 5861 for violation of such duties. The Constitution requires no more. The standard employed by the Supreme Court in reviewing penal statutes for certainty is whether they convey sufficiently definite warning as to the proscribed conduct when measured by common understanding and practice. *United States v. Petrillo*, 332 U.S. 1, 8.

Appellant has quoted from *United States v. Harris*, 347 U.S. 612, at page 617 (App. Br. 22) defining the constitutional requirement for definiteness in a criminal statute, but has neglected to include the paragraph following his printed excerpt. At page 618 the Court continues:

“On the other hand, if the general class of offenses to which the statute is directed is plainly within the terms, the statute will not be struck down as vague, even though marginal cases could be put where doubts might arise. *United States v. Petrillo*, 332 U.S. 1, 7. Cf. *Jordan v. DeGeorge*, 341 U.S. 223, 231. And if this general class of offenses can be made constitutionally definite by a reasonable construction of the statute, this court is under a duty to give the statute that construction. This was the course adopted in *Screws v. United States*, 325 U.S. 91, upholding the definiteness of the Civil Rights Act.”

The rule as to statutes charged with vagueness is but one aspect of the broader principle that the Court, if fairly possible, must construe Congressional enactments so as to avoid a danger of unconstitutionality. *United States v. Delaware & Hudson Co.*, 213 U.S. 366, 407-408; *United States v. Congress of Industrial Organizations*, 335 U.S. 106, 120-121; *United States v. Rumely*, 345 U.S. 41, 47.

Cases cited by appellants are inapposite, for in those cases the Court was called upon to examine into the definiteness of the precise statutes under which the defendants in each case were charged. Appellants here make no claim that the statutes under which they were charged are in any way vague or indefinite. Their sole claim is that Section 5846, which they have seized upon and injected into the case without showing they were misled thereby, somehow beclouds the otherwise clear course of conduct chartered in Chapter 53, Internal Revenue Code.

While appellants pose certain hypothetical questions in an effort to show that the statute is vague and misleading, they fail to show and do not claim that they were at any time misled as to their duties and responsibilities under the statute or that they attempted to chart a course which would comply with their understanding of the law. To the contrary, the evidence clearly shows that they were fully aware of the requirements that a tax be paid on the transfer of firearms; that an order form be prepared; and that the guns be registered (Tr. 115-118, 138, Vol. 2). Appellant von Eichelberger (who as transferor was

liable for the tax) admitted on cross-examination that the reason the order forms were not made out and the tax not paid was that he was financially unable to pay it (Tr. 122, Vol. 2). This is understandable, since the guns were sold by him for \$300 and the tax would have ranged from \$1600 to \$3000 depending on the number of weapons qualifying as firearms under the statute (Tr. 122, Vol. 2).

Section 5846 has no application to the charges contained in the indictment here and does not in any respect affect the statutes under which the indictment was returned.

III.

PROSECUTION OF APPELLANT VON EICHELBERGER ON COUNTS 17 TO 24 WAS NOT BARRED BY THE STATUTE OF LIMITATIONS.

Appellant von Eichelberger contends that the statute of limitations (Section 6531, Title 26 United States Code) bars prosecution on counts 17, 18, 20, 21, 22, 23 and 24.³ In these counts it is charged that appellant von Eichelberger "on or about the 5th day of December, 1956 and prior thereto, . . . did receive and possess" certain described machine guns which had been transferred to him in violation of Sections 5811 and 5814, Internal Revenue Code (Sections 5811 and 5814, Title 26, United States Code).

³Appellant assumes that the statute of limitations is six years, while we perceive it to be three years. Irrespective of which is correct, we concede that the statute of limitations has barred prosecution if appellant's theory is adopted.

The unlawful receipt or possession of a firearm is proscribed by Section 5851, Title 26, United States Code, which provides in part:

“It shall be unlawful for any person to receive or possess any firearm *which has at any time* been transferred in violation of Sections 5811, . . . 5814, . . . Whenever on trial for a violation of this section the defendant is shown to *have or to have had possession* of such firearm, such possession shall be deemed sufficient evidence to authorize conviction, unless the defendant explains such possession to the satisfaction of the jury.” (Italics supplied)

The penalty for violations of the above-quoted section is contained in Section 5861, Title 26 United States Code.

It is appellant von Eichelberger's contention that since his uncontradicted, but uncorroborated, oral testimony established that the machine guns in question were transferred to him prior to 1950, (concededly in violation of Sections 5811 and 5814) his criminal liability accrued from the dates of transfer and earlier than six years prior to the return of the indictment.

The evidence shows, and appellant von Eichelberger admitted, that he possessed the firearms in question on December 5, 1956, the date set forth in the indictment, and prior thereto (Tr. 97, 102, Vol. 2). That is the gist of the offense. In his argument appellant misconceives the nature of the charge against him in counts 17 to 24. He is not charged with failure to

pay the transfer tax or failure to use the order form in counts 17 to 24;—he is charged with *possession* of guns transferred to him without compliance with those provisions of the Internal Revenue Code. The statutory language clearly prohibits the present possession of a firearm thus unlawfully transferred, irrespective of the date of transfer. Any other construction would make meaningless the phrase “possess any firearm which has *at any time* been transferred” in Section 5851. The intent of Congress to prohibit possession of illegally transferred firearms is further evidenced by the presumption contained in Section 5851 and containing the language “Whenever . . . the defendant is shown *to have or to have had* possession . . . ” of illegally transferred firearms, such possession is sufficient to convict.

Concededly, prosecution for possession at a time earlier than three years prior to the return of the indictment would be barred by the statute of limitations. However, that is not the situation here, for the indictment was returned on March 6, 1957, only three months after the firearms were relinquished by appellant (Tr. 2, Vol. 1). Clearly, the possession of the firearms was well within the period allowed for institution of criminal proceedings. For, in general, the statute of limitations does not apply when some portion of the crime is within the period, although another portion thereof is not. 22 C.J.S. Criminal Law, Sec. 227.

The Courts do not appear to have been called upon to determine when the statute of limitations starts to

run under Section 5851, Internal Revenue Code. It is clear, however, that the possession of firearms unlawfully transferred is a separate and distinct offense from failure to pay the transfer tax, failure to use order forms, or possession of unregistered firearms. See, e.g.: *United States v. Hardgrave*, 214 F.2d 673 (C.A. 7th, 1954); *Montgomery v. United States*, 146 F.2d 142 (C.A. 4th, 1944); *Wright v. United States*, 243 F.2d 546 (C.A. 6th, 1957); *Rayborn v. United States*, 234 F.2d 368 (C.A. 6th, 1956).

Appellants' argument that his obligations and duties were fixed upon the transfer and receipt of the guns prior to 1950 finds no support in the foregoing cases, for they clearly consider the offenses to be separate and distinct ones. That the time and manner of original acquisition of the firearms is considered of no consequence is demonstrated by the *Rayborn* and *Montgomery* cases, *supra*, each of which dealt with prosecution for receipt and possession of firearms which had been stolen by the defendant. In neither case does the Court consider the dates of theft, but only whether the subsequent possession without compliance with the statutes constitutes properly charged offenses.

Applying the presumption contained in Section 5851, Title 26 United States Code to the facts here, it is uncontradicted that the appellant had had possession of the firearms described in the indictment within the period of the statute of limitations. In the absence of satisfactory explanation, such possession alone was sufficient evidence to support the conviction.

Finally, the argument advanced by appellants would frustrate the clear intent of Congress to control the traffic in deadly weapons such as machine guns, to limit the possession of such guns to qualified citizens, and to maintain a record of the persons who had such weapons in their possession. With such intent in mind, it is necessary to construe the offense as being committed during all times that the unlawful possession occurred. To hold that the offense was completed at the time of securing of the weapon, and that subsequent concealment for the period of the statute of limitations would relieve the possessor of the requirement to comply with the law, would reduce the situation to an absurdity. By its very nature, the act of possession in violation of the statute was a continuing one until such time as the weapons left the hands of the appellants. This occurred on December 5, 1956 and the statute of limitations began to run on that date alone.

IV.

THE SEARCH OF TROST'S GARAGE AND THE SEIZURE OF THE CONTRABAND FIREARMS DID NOT VIOLATE APPELLANTS' CONSTITUTIONAL RIGHTS.

Appellants contend that since they failed to give permission to the investigating agents to enter Trost's garage, and since no search warrant was issued, the search was unreasonable and the evidence thus obtained, consisting of the machine guns in question, was inadmissible against them. The government con-

tends that the case does not involve any search and seizure, illegal or otherwise.

a. **The Search Was With the Consent of the Legal Occupant of the Premises.**

At the outset it is clear that neither appellant had any authority to either grant or deny permission to enter Trost's garage. The premises were entirely under Trost's control; only Trost had the key; only Trost paid the rent; and only Trost was able to give permission to the agents to enter the garage (Tr. 13-19, 113-114; 132-133, Vol. 2). That the entry of the agents into Trost's garage was with his consent and by his invitation is conceded by appellants (App. Br. 27). No further permission was needed.

Appellants cannot complain that the incriminating evidence was taken from a third party—Trost, who willingly and voluntarily surrendered it to the agents (Tr. 23, Vol. 2). As this Court said in *Remmer v. United States*, 205 F.2d 277, 285, (reversed on other grounds 347 U.S. 227 and 350 U.S. 377): "The records . . . were obtained by the government from third parties rather than from appellant. Use of such records by the prosecution would not violate appellant's constitutional rights, even were it true that the third parties originally obtained the records from appellant illegally."

It has been held that a search without a warrant, but with consent of the person left in charge by the owner is lawful, (*United States v. Walker*, 197 F.2d 287 (C.A. 2d, 1952); cert. denied, 344 U.S. 877;

Raine v. United States, 299 Fed. 407, 411 (C.A. 9th, 1924); cert. denied, 266 U.S. 611), and that consent by a joint tenant, when the defendant and the consenting party both had free access to a garage, is not an “unreasonable” search and seizure (*Driskill v. United States*, 281 Fed. 146 (C.A. 9th, 1922)). To hold otherwise in this case, where only the consenting party (Trost) had free access to the premises; where the premises consisted of a garage; where no trespass, force, coercion or influence was employed by agents; and where the agents were invited to make a search, would “be to make of the constitutional provision a fetish, instead of a shield against the invasion of personal and property rights.” *Driskill v. United States*, 281 Fed. 146 (C.A. 9th, 1922).

b. Appellants Have No Interest in the Place Searched Sufficient to Give Them Standing to Complain.

Appellant Terzian claims a “right to possession” of the firearms, and a “license” in the premises on which they were stored as a result of Trost’s permission to use the premises for this sole purpose; and appellant von Eichelberger claims “ownership” of the guns (App. Br. 26). These claims are obviously an effort to establish some interest in the place searched and the property seized in order to bring appellants within the protection of the Fourth Amendment. It is axiomatic that if no rights of a defendant were disturbed, he is not aggrieved by an illegal search and seizure and cannot complain of the things seized in such a search being used against him. *United States v. Lee Hee*, 60 Fed. 2d 924, 926 (C.A. 2d, 1932). The privi-

lege cannot be claimed where the defendant disclaims ownership of the property seized, as appellant Terzian has done.

Ingram v. United States, 113 F.2d 966, 968 (C.A. 9th, 1940);

Driskill v. United States, 281 F. 146, 147 (C.A. 9th, 1922);

Kwong How v. United States, 71 F.2d 71, 75 (C.A. 9th, 1934).

Nor is mere physical custody of incriminating evidence enough to entitle one to invoke protection of the Fourth Amendment. *United States v. Mandell*, 17 F.2d 270, 273 (D.C. Mass., 1927).

This Court in *Kwong How v. United States*, 71 F.2d 71, 75 (1934) quoted with approval from *Kelley v. United States*, 61 F.2d 843, 846 (C.A. 8th, 1932) the following language:

“The question seems well settled . . . that one who is not the owner, lessee, or lawful occupant of the premises searched cannot raise the question under the Fourth Amendment of unlawful search and seizure.”

The most appellant Terzian claims is a “license” to use the property as a result of Trost’s permission to store boxes in the garage. This is clearly inadequate to give him standing to complain of a search of the premises and if allowed would extend the Constitutional protection to an extreme not previously envisioned. The result of such reasoning would be to require search warrants in every instance in which

the officers were unable to obtain consents to search from persons claiming some right or title in the property searched irrespective of whether they occupied the property. The absurdity of such logic is shown if instead of a private garage, the articles had been stored in a public warehouse.

Appellant von Eichelberger's argument is even more tenuous, for he is, in effect, contending that the protection of the Fourth Amendment follows the legal title in seized property, irrespective of who has custody or possession. He cites no cases for this proposition, and we have found none.

c. The Premises Searched, Consisting of a Garage, Fall Outside the Protection of the Fourth Amendment.

Even assuming, *arguendo*, that appellants have shown sufficient interest in the property seized to satisfy the Court, the premises searched, consisting of a garage, do not fall within the term "house" as used in the Fourth Amendment. *Carney v. United States*, 163 F.2d 784, 787 (C.A. 9th, 1947); cert. denied, 332 U.S. 824. Cf. *United States v. McBride*, 284 Fed. 416; cert. denied, 261 U.S. 614; *Hester v. United States*, 265 U.S. 57.

In *Martin v. United States*, 183 F.2d 436 (C.A. 4th, 1950), a garage was searched and untaxed liquor was found therein. A motion to suppress the evidence there obtained was denied. In *Johnson v. United States*, 199 F.2d 231 (C.A. 4th, 1952) a whole farm, including a truck outside the house, and a garage were

searched, and the Court held that such a search was reasonable.

In *Earl v. United States*, 4 F.2d 532 (C.A. 9th, 1925), the search was of a garage in the basement of a dwelling house, with which it was wholly unconnected, and which was leased to and occupied by other tenants. The Court held that the garage was not a "house" within the protection of the amendment. To the same effect are *Vaught v. United States*, 7 F.2d 370 (C.A. 9th, 1925) and *Gay v. United States*, 8 F.2d 219, 220 (C.A. 9th, 1925) where it was held that no search warrant was necessary for a garage.

If, as appears, appellants concede that the search of the garage was lawful, but contend that the subsequent search of the boxes containing the firearms was an invasion of their Constitutional rights (App. Br. 27) they are attempting to extend the protection of the Fourth Amendment to unreasonable extremes. None of the cases even remotely suggest the possibility that once a lawful entry has been gained, a search for contraband becomes unreasonable because it is not found in plain sight. To follow petitioners' reasoning to its illogical result would require the conclusion that a search warrant is needed in every case in which evidence is concealed. It would, for example, require a search warrant to break open a sealed envelope in which narcotics were contained. The Fourth Amendment does not compel such absurd results.

Petitioners cite *Marron v. United States*, 275 U.S. 192 as authority for this proposition, but the case is

inapposite. In that case the officers seized books and records which were not described in the search warrant, but which were admitted into evidence. The resulting conviction was affirmed by this Court and the Supreme Court.

Nor is *United States v. Jeffers*, 342 U.S. 48, cited by petitioners applicable to the facts here. In that case the initial entry of the officers into the hotel room of defendant's aunts was a trespass, whereas the entry here was by invitation of the occupant.

Clearly, no constitutional right of either appellant was violated and the evidence was properly admitted against them.

d. The Weapons Were Properly Seized as Contraband.

Finally, the firearms in question were subject to seizure and forfeiture pursuant to Section 5862 of Title 26, *United States Code*. The Supreme Court recognizes that a search for contraband presents a different problem than one which has as its object the private papers or effects of the defendant. *Boyd v. United States*, 116 U.S. 616, 624; *Davis v. United States*, 328 U.S. 582; *Harris v. United States*, 331 U.S. 145, 155. No agent of the United States is required to stand passively by while a crime is being committed in his presence. When the agents discovered the cache of machine guns they could not be expected to turn on their heels and walk out. It became their plain duty to seize the contraband, and no rule of evidence or constitutional privilege can bar the use of this

evidence to convict the defendants. It must be remembered that "a criminal prosecution is more than a game in which the government may be checkmated and the game lost merely because its officers have not played according to rule." *McGuire v. United States*, 273 U.S. 95, 97.

e. The Search and Seizure Was a Reasonable One.

The Fourth Amendment prohibits only "unreasonable" searches and seizures. The question of reasonableness is one peculiarly within the province of the trial judge. The trial judge is in a position to know the total atmosphere of the case. His determination of reasonableness should not be disturbed if fairly supported by the evidence. *Shelton v. United States*, 197 F.2d 827, 828 (C.A. 5th, 1952); *Davis v. United States*, supra, *Martin v. United States*, supra, "The test of reasonableness cannot be stated in rigid and absolute terms. It cannot be determined by any fixed formula; the recurring questions of the reasonableness of search must find resolution in the facts and circumstances of each case." *Harris v. United States*, supra. The government submits that under all the facts and circumstances the search and seizure in this case, if it be a search and seizure, was a reasonable one.

CONCLUSION.

For the reasons hereto set forth, it is respectfully submitted that the judgment of the District Court should be affirmed.

Dated, San Francisco, California,
October 18, 1957.

Respectfully submitted,

LLOYD H. BURKE,

United States Attorney,

JOHN LOCKLEY,

Assistant United States Attorney,

Attorneys for Appellee.

(Appendix Follows.)



Appendix.



Appendix

Internal Revenue Code of 1954 (Title 26, United States Code):

Sec. 5811. Tax.

(a) Rate. There shall be levied, collected, and paid on firearms transferred in the United States a tax at the rate of \$200 for each firearm: *Provided*, That the transfer tax on any gun with combination shotgun and rifle barrels, 12 inches or more but less than 18 inches in length, from which only a single discharge can be made from either barrel without manual reloading, or any gun designed to be held in one hand when fired and having a barrel 12 inches but less than 18 inches in length from which only a single discharge can be made without manual reloading, shall be at the rate of \$1. The tax imposed by this section shall be in addition to any import duty imposed on such firearm.

(b) By Whom Paid. Such tax shall be paid by the transferor.

(c) How Paid.

(1) Stamps. Payment of the tax herein provided shall be represented by appropriate stamps to be provided by the Secretary or his delegate.

Sec. 5814. Order Forms.

(a) General Requirements. It shall be unlawful for any person to transfer a firearm except in pur-

suance of a written order from the person seeking to obtain such article, on an application form issued in blank in duplicate for that purpose by the Secretary or his delegate. Such order shall identify the applicant by such means of identification as may be prescribed by regulations under this chapter: *Provided*, That, if the applicant is an individual, such identification shall include fingerprints and a photograph thereof.

(b) Contents of Order Form. Every person so transferring a firearm shall set forth in each copy of such order the manufacturer's number or other mark identifying such firearm, and shall forward a copy of such order to the Secretary or his delegate. The original thereof, with stamp affixed, shall be returned to the applicant.

(c) Documents to Accompany Transfers. No person shall transfer a firearm unless such person, in addition to complying with subsection (b), transfers therewith (in compliance with such regulations as may be prescribed under this chapter for proof of payment of all taxes on such firearm)

(1) for each prior transfer of such firearm which was subject to the tax imposed by section 5811(a), the stamp-affixed order provided in this section, and

(2) for any making of such firearm which was subject to the tax imposed by section 5821(a), the stamp-affixed declaration provided in section 5821.

Sec. 5846. Other Laws Applicable.

All provisions of law (including those relating to special taxes, to the assessment, collection, remission, and refund of internal revenue taxes, to the engraving, issuance, sale, accountability, cancellation, and distribution of taxpaid stamps provided for in the internal revenue laws, and to penalties) applicable with respect to the taxes imposed by sections 4701 and 4721, and all other provisions of the internal revenue laws shall, insofar as not inconsistent with the provisions of this chapter, be applicable with respect to the taxes imposed by sections 5811(a), 5821(a) and 5801.

Sec. 5848. Definitions.

For purposes of this chapter—

(10) To Transfer or Transferred. The term “to transfer” or “transferred” shall include to sell, assign, pledge, lease, loan, give away, or otherwise dispose of.

Sec. 5821. Possessing Firearms Unlawfully Transferred or Made.

It shall be unlawful for any person to receive or possess any firearm which has at any time been transferred in violation of sections 5811, 5812(b), 5813, 5814, 5844, or 5846, or which has at any time been made in violation of section 5821. Whenever on trial for a violation of this section the defendant is shown to have or to have had possession of such firearm, such

possession shall be deemed sufficient evidence to authorize conviction, unless the defendant explains such possession to the satisfaction of the jury.

Sec. 5861. Penalties.

Any person who violates or fails to comply with any of the requirements of this chapter shall, upon conviction, be fined not more than \$2,000, or be imprisoned for not more than 5 years, or both, in the discretion of the Court.

Sec. 5862. Forfeitures.

(a) Laws Applicable. Any firearm involved in any violation of the provisions of this chapter or any regulation promulgated thereunder shall be subject to seizure and forfeiture, and (except as provided in subsection (b)) all the provisions of internal revenue laws relating to searches, seizures, and forfeiture of unstamped articles are extended to and made to apply to the articles taxed under this chapter, and the persons to whom this chapter applies.

No. 15655

United States
Court of Appeals
for the Ninth Circuit

VIRGIL D. DARDI, Individually and as Executor
of the Estate of UMBERTO DARDI,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Appeal from the United States District Court for the
Northern District of California,
Southern Division.

FILED
SEP 13 1957

PAUL P. O'BRIEN, CLERK



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF COUNSEL

PHILLIPS, AVAKIAN and JOHNSTON,
J. RICHARD JOHNSTON, ESQ.,

Financial Center Building,
Fourteenth at Franklin Streets,
Oakland, 12, California,

For Appellant.

CHARLES H. RICE,
Assistant U. S. Attorney General;

LEE A. JACKSON,
Chief, Appellant Section, Dept. of Justice,
Washington, 25, D.C.,

LLOYD H. BURKE, ESQ.,
United States Attorney;

C. ELMER COLLETT,
Assistant United States Attorney,
Post Office Building,
San Francisco, California,

For Appellee.



In the United States District Court for the Northern
District of California, Southern Division

Civil No. 34297

UNITED STATES OF AMERICA,

Plaintiff,

vs.

THE MISSION COMPANY; VIRGIL D. DARDI,
Individually and as Executor of the Estate of
UMBERTO DARDI; and OLGA PAULA as
Trustee of Trust for JOSEPH DARDI and as
Trustee of Trust for MARY CLAIRE ELE-
VITA DARDI,

Defendants.

COMPLAINT

The United States of America, by Lloyd H. Burke,
United States Attorney for the Northern District of
California, for its complaint against the above-named
defendants alleges as follows:

I.

That at all times hereinafter mentioned the plain-
tiff was and now is a sovereign body politic.

II.

That this is an action arising under the laws of the
United States providing for the internal revenue
and the collection thereof.

III.

That this action has been authorized by the Attor-
ney General of the United States at the request of the
Commissioner of Internal Revenue.

IX.

On information and belief, that on or about June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi, each as owner of fifty per cent of the stock of the defendant The Mission Company, received as a distribution from The Mission Company all of its assets which had a value in excess of the tax liability asserted herein without giving anything of value in return therefore at a time when the defendant The Mission Company either was insolvent or by virtue of the said distribution was rendered insolvent.

X.

On information and belief, that subsequent to June 30, 1943, defendant Virgil D. Dardi formed a partnership or other business venture with Umberto Dardi, and transferred thereto the assets received from the defendant The Mission Company, as specified in paragraph IX, and thereafter used such assets in the operation of two businesses, to wit; Cigar Box Restaurant and All-American Creamery, both being located within the city of San Francisco, California.

XI.

On information and belief, that subsequent to June 30, 1943, defendant Virgil D. Dardi, transferred his interest in the partnership or other business venture alleged in paragraph X, or in the assets received from the defendant The Mission Company, as specified in paragraph IX, to two trusts for his children, to wit: Trust for Joseph Dardi and Trust for Mary Claire Elevita Dardi, without receiving anything of value therefor.

XII.

On information and belief, that Umberto Dardi died on or about April, 1948.

XIII.

On information and belief, that defendants Virgil D. Dardi, as the executor of the estate of Umberto Dardi, and Olga Paula, as the trustee of the trusts for Joseph and Mary Claire Elevita Dardi, are operating the Cigar Box Restaurant and the All-American Creamery as partners or co-venturers.

XIV.

On information and belief that the parties named herein are all of the persons who have or claim to have any interest in the property described herein.

XV.

That the claims and tax liens of the plaintiff, United States of America, are entitled to priority of payment out of the property described herein over the interests of all other parties in the said property.

Wherefore, the plaintiff prays:

1. That the Court enter judgment in favor of the United States of America against The Mission Company in the amount of \$15,983.60, plus interest and costs as provided by law.

2. That the Court adjudge, order and decree that the property and things of value taken over by defendant Virgil D. Dardi and by Umberto Dardi from the defendant The Mission Company, constitute a trust fund for the payment of the taxes and interest

asserted herein, and that the said property and things of value be applied to the payment of the said taxes and interest. Further, that if the application of the said property or things of value in payment of the taxes and interest asserted herein does not fully discharge the claim for the said taxes and interest, then the defendant United States of America to have judgment against Virgil D. Dardi, individually and as executor of the estate of Umberto Dardi, in the amount of the said taxes and interest still remaining due.

3. That this Court adjudicate all matters involved herein and finally determine the merits of all claims to and liens upon the property and rights to property described herein, and decree that the lien of the plaintiff is prior, senior and superior to any and all liens upon the property or rights to property described herein and that unless the taxes described herein are immediately paid, that the said property be sold by the proper officer of this Court and the proceeds of such sale be distributed first in satisfaction of plaintiff's lien for taxes, interest and penalties.

4. That the plaintiff have such other and further relief as to the Court may seem just and proper in the premises, together with the costs and disbursements of this action.

/s/ LLOYD H. BURKE,

United States Attorney,
Attorney for Plaintiff.

[Endorsed]: Filed December 15, 1954.

[Title of District Court and Cause.]

AMENDED ANSWER OF DEFENDANT
VIRGIL D. DARDI, INDIVIDUALLY

Now comes the defendant Virgil D. Dardi, individually, and in answer to the complaint on file herein admits, denies and alleges as follows:

I.

Admits the allegations of Paragraphs I, II, III, IV, V, VI, VII and XII.

II.

In answer to Paragraphs VIII, XIV, and XV, states that he is without knowledge or information sufficient to form a belief as to the truth of the allegations stated in those paragraphs.

III.

In answer to Paragraph IX, admits that assets of The Mission Company were transferred to him and Umberto Dardi, but states that he is without knowledge or information sufficient to form a belief as to the truth of the allegation that such assets had a value in excess of the tax liability asserted in the complaint, or the allegation that the alleged distribution was made at a time when The Mission Company either was insolvent or that by virtue of said distribution it was rendered insolvent; and denies the other allegations of said paragraph.

IV.

In answer to Paragraph X, denies the allegation that assets were received from The Mission Company "as specified in paragraph IX," and admits the other allegations of said paragraph.

V.

Denies the allegations of Paragraph XI.

VI.

In answer to Paragraph XIII, denies the allegation that this defendant or any defendant is presently operating the All-American Creamery as partners, co-venturers, or otherwise, or has so operated the All-American Creamery since about 1943; and admits the other allegations of said paragraph.

As a first affirmative defense, this defendant alleges as follows:

VII.

That at the time assets of The Mission Company were transferred to him, said corporation was indebted to this defendant in the sum of \$13,983.12, and said assets were transferred to this defendant and received by him as payment or partial payment of said indebtedness and not as a distribution to him as a shareholder.

As a second affirmative defense, this defendant alleges as follows:

VIII.

That the right of action set forth in the complaint did not accrue within six years next before the commencement of this action, and this defendant did

not agree to any extension of the period of limitations applicable to this action.

Wherefore, this defendant prays that plaintiff take nothing by this action and that he be dismissed hence with his costs.

Dated: February 20, 1956.

PHILLIPS, AVAKIAN &
JOHNSTON,

By /s/ J. RICHARD JOHNSTON,
Attorneys for Defendant.

Affidavit of service by mail attached.

[Endorsed]: Filed February 21, 1956.

[Title of District Court and Cause.]

AMENDED ANSWER OF DEFENDANT VIR-
GIL D. DARDI AS EXECUTOR OF THE
ESTATE OF UMBERTO DARDI

Now comes the defendant Virgil D. Dardi as Executor of the Estate of Umberto Dardi, and in answer to the complaint on file herein admits, denies and alleges as follows:

I.

Admits the allegations of Paragraphs I, II, III, IV, V, VI, VII and XII.

II.

In answer to Paragraphs VIII, XIV and XV, states that he is without knowledge or information

sufficient to form a belief as to the truth of the allegations stated in those paragraphs.

III.

In answer to Paragraph IX, admits that assets of The Mission Company were transferred to the defendant Virgil D. Dardi, individually, and to Umberto Dardi, but states that he is without knowledge or information sufficient to form a belief as to the truth of the allegation that such assets had a value in excess of the tax liability asserted in the complaint, or the allegation that the alleged distribution was made at a time when The Mission Company either was insolvent or that by virtue of said distribution it was rendered insolvent; and denies the other allegations of said paragraph.

IV.

In answer to Paragraph X, denies the allegation that assets were received from The Mission Company "as specified in Paragraph IX," and admits the other allegations of said paragraph.

V.

Denies the allegations of Paragraph XI.

VI.

In answer to Paragraph XIII, denies the allegation that this defendant or any defendant is presently operating the All-American Creamery as partners, co-venturers or otherwise, or has so operated the All-American Creamery since about 1943; and admits the other allegations of said paragraph.

As a separate affirmative defense, this defendant alleges as follows:

VII.

That the right of action set forth in the complaint did not accrue within six years next before the commencement of this action, and this defendant did not agree to any extension of the period of limitations applicable to this action.

Wherefore, this defendant prays that plaintiff take nothing by this action and that he be dismissed hence with his costs.

Dated: February 20, 1956.

PHILLIPS, AVAKIAN &
JOHNSTON,

By /s/ J. RICHARD JOHNSTON,
Attorneys for Defendant.

Affidavit of service by mail attached.

[Endorsed]: Filed February 21, 1956.

[Title of District Court and Cause.]

PRETRIAL ORDER

The above-entitled action having come on for pretrial conference on Wednesday, February 15, 1956, the following facts were agreed to by all the respective parties, and such facts are no longer in issue:

1. At all times hereinafter mentioned the plaintiff was, and now is, a sovereign body politic.

2. This is an action arising under the laws of the United States providing for the internal revenue and the collection thereof.

3. This action has been authorized by the Attorney General of the United States at the request of the Commissioner of Internal Revenue.

4. The Mission Company is a corporation organized under the laws of the State of California and at all times relevant to this action was doing business at 2200 Mission Street, San Francisco, California.

5. The defendants, Virgil D. Dardi and Olga Paula, are residents of San Francisco, California, or other places within the jurisdiction of this Court.

6. The Mission Company was incorporated under the laws of the State of California in January, 1941, under the name of Dardi and Company; in April, 1941, said corporate name was changed to R. J. Howell, Inc.; in November, 1942, said corporate name was changed to The Mission Company.

7. The Mission Company filed corporate income tax returns for the calendar year 1942 and for the period January 1, 1943, to June 30, 1943; said returns were filed by Virgil D. Dardi as president and Umberto Dardi as vice president.

8. Income and excess profits taxes were assessed against The Mission Company as follows:

Year	Tax	Amt. Assessed	Post War Credit	Amt. Owed
1942	E.P.	\$8,117.06	\$811.71	\$ 7,305.35
1942	I.T.	14.50		369.96
	Int.	3.47		
	DVEP	283.99		
	Int.	68.00		
1943	E.P.	6,305.04	630.50	5,674.54
1943	I.T.	726.05		2,633.75
	Int.	130.28		
	DVEP	1,507.01		
	Int.	270.41		
				<hr/> \$15,983.60

The assessment list pertaining to the above tax liabilities was signed by the Commissioner of Internal Revenue on October 10, 1947, and received by the Collector of Internal Revenue at San Francisco on October 13, 1947, on which date a lien of the plaintiff, United States of America, arose on all property and rights to property of The Mission Company; said assessment was within the applicable statute of limitations for assessment of such taxes as duly extended by Virgil D. Dardi as president of The Mission Company; notice and demand was made on The Mission Company on October 17, 1947; no part of the \$15,983.60, plus interest, due to the United States of America for the above taxes has been paid; waivers were executed by Virgil D. Dardi as president of The Mission Company on October 21, 1952, extending the time of collection of the above tax liabilities by distraint or by proceedings in court until December 31, 1956; notices of Federal tax liens were filed pursuant to Section 3672 of the Internal Revenue Code of 1939 for the tax liabilities asserted

herein in the County of San Francisco, California, on January 9, 1948, in the amount of \$19,491.39.

9. No waiver extending the time of collection of the above tax liabilities by distraint or by proceedings in court has ever been executed by Virgil D. Dardi, either individually or as executor of the estate of Umberto Dardi, or by Olga Paula as trustee of the trust for Joseph Dardi or as trustee of the trust for Mary Claire Elevita Dardi.

10. On or about June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi each received from The Mission Company one-half of its assets. Subsequent to June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi formed a partnership, transferred thereto the assets which they had received from the defendant, The Mission Company, and thereafter used such assets in the operation of two businesses, to wit: Cigar Box Restaurant and All-American Creamery, both being located within the City of San Francisco, California.

11. On or about April 30, 1944, Virgil D. Dardi transferred his interest in the partnership known as "The Mission Co." to Eugene Engle. On or about January 1, 1945, Eugene Engle in turn transferred such interest to John Clifton Ernst, in trust for the benefit of Joseph Dardi and Mary Claire Elevita Dardi.

12. Umberto Dardi died on or about April, 1948.

13. The defendant, Virgil D. Dardi, as executor of the estate of Umberto Dardi, and the defendant,

Olga Paula, as trustee of the trusts for Joseph and Mary Claire Elevita Dardi, are operating the Cigar Box Restaurant as partners or co-venturers.

It was further agreed among the respective parties to this action that the following questions are in issue:

1. Whether the instant suit has been timely commenced against the defendants, Virgil D. Dardi, individually and as executor of the estate of Umberto Dardi, and Olga Paula as trustee for the trusts for Joseph Dardi and Mary Claire Elevita Dardi.

2. Whether the transfer of assets from The Mission Company to Virgil D. Dardi and Umberto Dardi was for good and valuable consideration.

3. Whether the transfer of assets from The Mission Company to Virgil D. Dardi and Umberto Dardi was at a time when the defendant, The Mission Company, was either insolvent, or by virtue of said transfer of assets was thereby rendered insolvent.

4. The value of the assets transferred from The Mission Company to Virgil D. Dardi and Umberto Dardi.

5. Whether the transfer of the interest of Virgil D. Dardi in the partnership referred to as the "Cigar Box Restaurant" to Eugene Engle was a bona fide transfer for good and valuable consideration.

6. Whether the transfer of the interest of Eugene Engle in the partnership referred to as the "Cigar Box Restaurant" to the trustee for the trusts for Joseph Dardi and Mary Claire Elevita Dardi was a bona fide transfer for good and valuable consideration.

/s/ MICHAEL J. ROCHE,
United States District Court
Judge.

Approved:

/s/ J. RICHARD JOHNSTON,
Attorney for Defendants.

/s/ JOSEPH O. GREAVES,
Attorney for Plaintiff.

[Endorsed]: Filed March 6, 1956.

[Title of District Court and Cause.]

MOTION FOR JUDGMENT ON THE
PLEADINGS

Defendants Virgil D. Dardi, both individually and as executor of the estate of Umberto Dardi, and Olga Paula as trustee of trust for Joseph Dardi and as trustee of trust for Mary Claire Elevita Dardi, move for judgment on the pleadings in their favor on the ground that this action is barred by the statute of limitations, since it was commenced more than six years after the right of action accrued and

said defendants did not agree to any extension of the applicable period of limitations.

Dated: March 26, 1956.

PHILLIPS, AVAKIAN &
JOHNSTON,

By /s/ J. RICHARD JOHNSTON,
Attorneys for Defendants.

Affidavit of Service by Mail attached.

[Endorsed]: Filed March 28, 1956.

[Title of District Court and Cause.]

ORDER

Upon the authority of the case of United States vs. City of New York, et al., S.D.N.Y., 134 F. Supp. 374, the reasoning of which case appears to the Court to be sound, it is hereby ordered that the motion of the defendant for judgment on the pleadings be, and the same hereby is, denied.

Dated: April 13, 1956.

/s/ O. D. HAMLIN,
United States District Judge.

[Endorsed]: Filed April 13, 1956.

[Title of District Court and Cause.]

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, and their respective counsel of record, that the following facts should be taken as true :

(1) The defendant corporation, The Mission Company, was incorporated in January, 1941, under the name of Dardi & Co., which name was changed to R. J. Howell, Inc., in April, 1941, which name was changed to The Mission Company in November, 1942. Said corporation had an authorized capital of 5,000 shares of \$1.00 par value stock, but no stock in said corporation was ever issued. The defendant Virgil D. Dardi, was the president and Umberto Dardi was the vice president. The corporation owned and operated a restaurant known as the Cigar Box Restaurant.

(2) Attached hereto as Exhibit A is a copy of a balance sheet of the corporation as of June 30, 1943, which was prepared from the corporate books. Attached hereto as Exhibit B is a copy of a balance sheet of said corporation which was filed with its corporation income and declared value excess profits tax return for the calendar year 1942, which return was filed by Virgil D. Dardi as president and by Umberto Dardi as vice president of The Mission Company.

(3) On June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi each received from The Mission

Company one-half of its assets and said Virgil D. Dardi and Umberto Dardi assumed the liabilities of said corporation as shown on its books at that date. On June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi formed a partnership known as The Mission Co., to which they transferred the assets which they had received and the liabilities which they had assumed from the defendant The Mission Company. Said partnership thereafter continued to operate the business known as the Cigar Box Restaurant.

(4) Attached hereto as Exhibit C is a copy of a balance sheet of said partnership, prepared from its books as of June 30, 1943.

(5) No consideration passed from said partnership to said corporation for the transfer of the assets of the latter to the former, except as the assumption of the liabilities above referred to may constitute such a consideration.

(6) On or about April 30, 1944, Virgil D. Dardi transferred his interest in the partnership known as The Mission Co. to Eugene Engle. This transfer was evidenced by a bill of sale dated April 28, 1944, a photocopy of which is attached hereto, as Exhibit D. In consideration for this partnership interest, Eugene Engle executed and delivered to Virgil D. Dardi his promissory note dated April 30, 1944, in the sum of \$150,000.00, a photocopy of which is attached hereto as Exhibit E. This note provided for installment payments as follows:

\$27,000 on or before December 31, 1944;
\$30,000 on or before December 31, 1945;
\$30,000 on or before December 31, 1946;
Balance on or before December 31, 1947.

(7) Eugene Engle paid Virgil D. Dardi the sum of \$27,900.00 in 1944, in payment of the first installment due on said note, and Virgil D. Dardi reported the receipt of this payment in his individual Federal income tax return for the year 1944.

(8) On or about January 1, 1945, Eugene Engle transferred his 50% partnership interest in The Mission Co. to John Clifton Ernst, as trustee for Mary Claire Dardi and Joseph Dardi, the two minor children of Virgil D. Dardi. This transfer was evidenced by a trust indenture which was duly executed by the parties, and a photocopy of which is attached hereto as Exhibit F. Pursuant to this trust indenture, the trustee made payments to Virgil D. Dardi in the amounts set forth below, and Virgil D. Dardi reported the receipt of such payments in his individual Federal income tax returns for the respective years in which the payments were made:

1945	\$21,169.06
1946	\$38,175.00

(9) On or about May 6, 1947, Virgil D. Dardi executed a release, discharging Eugene Engle from any further liability under his note of April 30, 1944. A photocopy of this release is attached hereto as Exhibit G.

(10) If Virgil D. Dardi and Eugene Engle were called to testify as witnesses in this suit, they would testify that they participated in these transactions in good faith and that the transactions were real, not sham.

Dated this 2nd day of April, 1957.

LLOYD H. BURKE,
United States Attorney;

/s/ LYNN J. GILLARD,

By /s/ JOSEPH O. GREAVES,
Attorney, Office of Regional Counsel, Internal
Revenue Service, Attorneys for Plaintiff.

/s/ J. RICHARD JOHNSTON,
Attorneys for All Defendants.



THE MISSION CO., INC.
 DEPARTMENTAL BALANCE SHEET
 JUNE 30, 1943.

CURRENT ASSETS:	CREAMERY		ELIMINATIONS		COMBINED
	RESTAURANT	CREAMERY	DR	CR	
CASH					
CASH ON HAND	\$5443	\$797			\$5840
CHANGE FUND	5000	4000			9000
SAVINGS ACCOUNTS	74314				74314
COMMERCIAL DEPOSITS	7444	13460			5676
TOTAL	\$71713	\$13875			\$86740
MERCHANDISE INVENTORY	274280	45000			319080
DEPOSITS	710000	55050			765050
A/R - CREAMERY	726461		726461		-
MARKETABLE SECURITIES	44450				44450
TOTAL CURRENT ASSETS	1494450	72807			1496780
FIXED ASSETS:					
FURN. FIXT. & EQUIP	\$1173413	710000			1873413
LESS: RESERVE FOR DEPR.	29507	181873			422380
	88411	528107			1410418
AUTO	19125	-			19125
TOTAL FIXED ASSETS	1074635	548107			1601143
OTHER ASSETS:					
INVESTMENT IN GENE'S	700000				700000
GOODWILL	54224				54224
TOTAL ASSETS	\$3483814	\$76444			\$3813765
LIABILITIES & CAPITAL					
LIABILITIES:					
ACCOUNTS PAYABLE	\$836953	\$74007	736461		\$911499
NOTES PAYABLE	775344				775344
ACCURED PAYROLL	700165	700165			704780
V. DARDI	138076				138076
ACCURED TAXES	162167	72807			192074
TOTAL LIABILITIES	7099749	367877			7511165
CAPITAL LOAN:					
V. DARDI-INVESTMENT	1044454	387260			1431814
" " WITHDRAWALS	-	33500			33500
SURPLUS-1-1-43	\$51746	52634			44982
PROFIT OR LOSS	1721	17301			26434
SURPLUS-6-30-43	139611	44477			184088
TOTAL LIABILITIES & CAPITAL	\$3483814	\$76444			\$3813765

(WITHOUT AUDIT)



Cash
 deposits
 Merchandise donations
 Furniture and fixtures
 Reserve for special
 account payable - all American Company
 Automobile
 Miscellaneous
 Investment - Bonds
 Goodwill

Total

Accounts payable
 Accounts payable - U. S. Bonds
 Accounts payable - all American Company
 Notes payable
 Accounts payable - all American Company
 Accounts payable - all American Company
 Accounts payable - all American Company

Accounts payable
 California - all American Company
 U. S. Bonds - all American Company
 Note with
 surplus
 U. S. Bonds - all American Company
 U. S. Bonds - all American Company

Total

1. Includes payable to Capital Ave. Co.
 all American Company

87470
 75560
 31980
 1983613
 231661
 151525
 44680
 5000 -
 511345

405000

1159960

138000

61760

77544

20480

7740

4141

200 -

19529

6670

< 835 -

670903

670904

405000

EXHIBIT D

Bill of Sale

Know All Men by These Presents, that I, the undersigned Virgil Dardi, of the City and County of San Francisco, State of California, do hereby sell, assign, and set over as of this day for good and valuable consideration to Eugene Engel, of the City and County of San Francisco, State of California, all of my right, title and interest in and to the business known and designated as the Mission Co., being a club and restaurant conducted at 2202 Mission Street, San Francisco, California, and do likewise by these presents sell, assign, and transfer and set over to the said Eugene Engel all of my right, title and interest in and to said furnishings and fixtures, stock in trade, accounts receivable, leases and all other personal property and equipment now located in the said premises occupied by the said club and restaurant therein described.

In Witness Whereof, I have set my hand on this 28th day of April, 1944.

/s/ VIRGIL DARDI.

EXHIBIT E

\$150,000.00

San Francisco, California
April 30, 1944

For Value Received, I promise to pay to Virgil D. Dardi or order, at San Francisco, California, the principal sum of One Hundred Fifty Thousand and No/100 (\$150,000.00) Dollars in lawful money

of the United States, with interest thereon in lawful money of the United States from date hereof and until paid, at the rate of three (3) per cent per annum.

And I further promise to pay said principal sum and interest as aforesaid, in installments as follows, to wit: Twenty-Seven Thousand Nine Hundred (\$27,900.00) Dollars thereof on or before the 31st day of December, 1944; Thirty Thousand Dollars (\$30,000.00) thereof on or before the 31st day of December, 1945; Thirty Thousand (\$30,000.00) Dollars thereof on or before the 31st day of December, 1946, and the balance, together with interest thereon, on or before the 31st day of December, 1947.

And I agree that in case of default in the payment of said interest as the same shall become due, then such interest so in default shall be added to and become a part of the principal and thereafter bear the same rate of interest; and at any time during default in the payment of said interest or in the payment of any installment of principal in the manner aforesaid, the entire unpaid balance of said principal and the interest thereon, shall, at the option of the holder of this note, be due and payable without notice.

/s/ E. J. ENGLE.

EXHIBIT F

Trust Indenture

This Trust Indenture, made and entered into this first day of January, 1945, by and between Eugene Engle, of the City and County of San Francisco,

State of California, hereinafter called the "Donor," first party hereto, and John Clifton Ernst, of the City and County of San Francisco, State of California, hereinafter called the "Trustee," second party hereto.

Witnesseth

That the Donor, for and in consideration of the agreement of the Trustee to undertake and perform the duties of Trustee as hereinafter provided, does hereby give, grant, convey, transfer, assign, set over and deliver to said Trustee and to his successor or successors as Trustee hereunder, as a gift to and for the benefit of Mary Claire Dardi and Joseph Dardi, all his right, title and interest of every kind and character in and to that certain partnership composed of Umberto Dardi and himself, doing business under the firm name and style of Mission Company, which interest Donor represents to be an undivided one-half therein as reflected in the audited Asset and Liability Statement of the partnership dated December 31, 1944, attached hereto and marked Exhibit "A," and which said interest is subject to an indebtedness in the sum of \$122,100.00 owing by Donor to Virgil D. Dardi.

In Trust, Nevertheless, for the term and for the uses and purposes hereinafter set forth:

First: Immediately after the creation of the trusts provided for herein or as soon thereafter as is possible, the Trustee shall assume, as Trustee only, the present existing indebtedness in the sum of \$122,-

100.00 owing from Donor to Virgil D. Dardi, as evidenced by that certain promissory note dated April 30, 1944, executed by the Donor to Virgil D. Dardi, in the face amount of \$150,000.00, together with interest thereon at the rate of three per cent (3%), and shall make every effort to secure from said Virgil D. Dardi the release of Donor from such indebtedness and from any and all liability which he may have or now has by reason thereof to said Virgil D. Dardi, and, as such Trustee, shall make, execute and deliver such evidences of indebtedness, notes, or other documents, and give such security therefor as the Trustee shall in his sole discretion deem necessary to effect such release. In carrying out the transactions provided for in this paragraph the Trustee shall incur no personal liability.

Second: The Trustee is authorized to permit the interest of Donor in the said partnership to remain employed in the business of such partnership upon such terms and conditions, either those by law implied or as may be expressly agreed upon with the remaining partner, as the Trustee may deem advisable, and said Trustee shall not be personally liable for any loss incurred in the conduct of such business not due to wilful default or misconduct. Trustee is further empowered to authorize the remaining partner in conjunction with the Trustee, as such Trustee, to continue to carry on and conduct the business of such partnership to the extent permitted by law. Should the Trustee at any time

determine in his sole and absolute discretion that the business cannot be continued to the advantage of the trust estates, he may sell or dispose of the same in the manner deemed by him to be for the best interest of the trust estates. In this connection, if it be deemed expedient to change the form of business from partnership to corporation or to any other form of business, the Trustee shall have full power to cause the interest of the Donor in and to the partnership and all property and assets used in connection therewith to be transferred to a corporation, the shares of which shall be held by the Trustee subject to the provisions of this indenture; provided, however, that should it become necessary for the Trustee to sell or dispose of all or any part of the shares of stock for the purpose of carrying out the provisions of the trusts, Trustee shall first offer such shares as are to be sold or disposed of to Virgil D. Dardi at the then fair market value of such shares.

Third: The Trustee shall divide the trust estate into two equal shares, setting aside one such share for Mary Claire Dardi and one such share for Joseph Dardi, and shall collect and receive the income of each of said trusts and the rents, issues and profits thereof and therefrom and shall apply the net income and principal of each trust estate as follows:

(a) From the net income thereof the Trustee shall first pay the indebtedness to which the principal of the trusts herein created is subject in the manner and as called for under the terms and pro-

visions of that certain promissory note dated April 30, 1944, executed by Donor to Virgil D. Dardi, or of such instrument or instruments as may be substituted therefor by the Trustee as such Trustee. The remainder of the net income, if any, or, should such indebtedness be fully discharged prior to the termination of the trusts, as herein provided, the entire net income, shall be paid to Mary Claire Dardi and Joseph Dardi, share and share alike.

(b) Upon the death of said Virgil D. Dardi, these trusts, subject to their or its possible continuance in trust as hereinafter provided, shall cease and terminate, and each trust estate, subject, however, to the remaining indebtedness, if any, to said Virgil D. Dardi, shall thereupon vest in, go and be transferred to Mary Claire Dardi and Joseph Dardi, or to the surviving issue, if any, of either of them then deceased by right of representation, or to the survivor of them should either of them be deceased leaving no issue, and should both be then deceased, neither of them leaving issue them surviving, then to their respective heirs at law, provided, however, that should either of the said beneficiaries become entitled to his or her respective trust estate before having attained the age of thirty years, then and in that event such share shall be continued in trust for such beneficiaries, under the following terms:

1. During the continuance of each such trust, the Trustee shall pay to or expend for and on behalf of the beneficiary whose trust is being continued the remainder of the net income, if any, of the trust estate, derived therefrom, after payment of the in-

debtedness herein referred to or the entire net income derived from such share should such indebtedness be fully discharged.

2. Each trust shall cease and terminate when the beneficiary for whose use and benefit such trust is being continued shall have attained the age of thirty years, or upon the death of any beneficiary prior to attaining that age, and thereupon such trust estate shall vest in, go and be transferred to that beneficiary should that beneficiary then survive, or to the then surviving issue, if any, of that beneficiary by right of representation, should that beneficiary be then deceased. But should no issue of that beneficiary then survive, and if the other said beneficiary shall not have attained the age of thirty years, it shall be added to and become a part of the trust being administered for that beneficiary, but if the other beneficiary shall have attained the age of thirty years then the said trust estate shall vest in, go and be transferred to said beneficiary should that beneficiary then survive, or to the surviving issue, if any of that beneficiary by right of representation, should that beneficiary be then deceased. And should both of said beneficiaries be then deceased, neither of them leaving issue them surviving, then to the respective heirs at law of each beneficiary, provided, however, should the survivor become entitled before having attained the age of thirty years to an additional share of the trust estate by reason of the death of one of said beneficiaries, then and in that event such ad-

ditional share shall be added to the trust estate being continued in trust for such surviving beneficiary, provided, further, however, that no trust herein created shall extend beyond the death of the last to die of Virgil D. Dardi, Mary Claire Dardi, and Joseph Dardi.

(c) Upon the death of any beneficiary theretofore receiving income payments hereunder, there shall be no apportionment of any income then accrued or accumulated from the trust estates but not yet paid between the heirs or legatees of such beneficiary and the beneficiary or beneficiaries next entitled to receive income and/or principal of the trust estates hereunder, but any and all such accrued, accumulated and unpaid income shall be paid to the beneficiary or beneficiaries next entitled to receive the income and/or principal of the trust estates hereunder.

(d) Should that portion of the net income payable to Mary Claire Dardi and Joseph Dardi at any time be deemed insufficient in the sole and absolute discretion of the Trustee, for the proper care, maintenance, support and education of the beneficiary then entitled to receive such share of the net income, then and in that event the Trustee shall pay to or expend for and on behalf of such beneficiary, in addition to such share of the net income, such portions of the principal of the respective trust estate as he shall deem necessary in his sole and absolute discretion for any of the aforesaid purposes, including all of the needs of that person occasioned or incurred by reason of sickness, accident, hospitaliza-

tion or other emergency, and in the exercise of such discretionary power the trustee shall be liberal.

(e) All income or principal to be paid to any of the beneficiaries named herein shall be paid by the Trustee direct, and only to said beneficiaries. The trustee is not to recognize any transfer, mortgage, pledge, hypothecation, order or assignment of any beneficiary by way of anticipation of any part of the income or principal. The principal and income of the trust estate shall not be subject in any manner to transfer by operation of law unless otherwise herein provided, and shall be exempt from the claims of creditors or other claimants, and from orders, decrees, levies, attachments, garnishments and executions, and other legal or equitable process or proceedings to the fullest extent permissible by law.

(f) The Trustee shall not be required to make an actual division of the trust estate pursuant to any provision of this agreement, except insofar as may be necessary on a whole or partial distribution of the trusts, but in his discretion he may hold, administer and invest the several shares of the trust estate as one or more common funds and may assign undivided interests in said common fund or funds to the several shares and divide the net income therefrom among the beneficiaries thereof proportionately.

Fourth: In addition to the powers granted to the Trustee in this instrument, the Trustee shall have the following powers:

(a) Subject to limitations, if any, states elsewhere in this indenture, the Trustee shall have every right and power in relation thereto and the assets thereof which any unmarried person could have as the absolute and unqualified owner, including full power to conclusively determine that which is income, net or gross, and to so determine that which is income or principal. He shall also have full power to invest and reinvest the assets of the trusts in, or to retain as such so long as he deems advisable, any property, real or personal, of any kind whatsoever, without responsibility for decline in value, regardless of whether such property shall be legal, or of a character appropriate for the investment of trust assets.

(b) The Trustee shall pay out of the gross income of the trust estates, or if said income be insufficient, then the balance thereof out of the principal, all taxes, assessments, insurance, costs, fees and expenses of every kind and nature, incurred or expended in the collection, care, administration, protection or distribution of the trust estates for the payment of which the trust estates and/or the Trustee may become chargeable, including a reasonable compensation to the Trustee for his services as such Trustee.

(c) The Trustee shall have the power, with respect to the trust estates, and upon such terms and in such manner as he may deem advisable, in his sole and absolute discretion, except as hereinafter provided, to sell for cash or upon installment terms, convey, exchange, grant options, convert, improve,

repair, manage, operate, cultivate and control; to lease for terms within or extending beyond the duration of the trusts and for any purpose, including the exploration for and removal of gas, oil and other minerals, with or without order of court; to borrow money, and to encumber or hypothecate by mortgage, deed of trust, pledge or otherwise; to carry insurance of such kind and in such amounts as the Trustee may deem advisable at the expense of the trusts, including public liability insurance for the protection of the Trustee, to compromise, settle or otherwise adjust any claim against or in favor of the trust; to sue for and/or defend for and on behalf of the trust estates as determined by the Trustee, in his sole and absolute discretion; and all costs, attorneys' fees and reasonable compensation to the Trustee in connection therewith shall be a charge against the trust estates, to enforce and collect all notes, mortgages, bonds, deeds of trust or other choses in action at any time constituting a part of the trust estates; to renew or extend the time of payment of any obligation due or becoming due to these trust estates; to foreclose by judicial proceedings or otherwise any security belonging to these trust estates; to invest and reinvest the trust estates or any portion thereof in such securities or other property as the Trustee may deem advisable, in his sole and absolute discretion, except as herein provided, whether or not of the character permitted by law for the investment of trust funds in the State of California; to make, execute and

deliver proxies; to hold title in the name of its nominee; to exercise and/or sell rights, to participate in foreclosures, reorganizations, consolidations, mergers and/or liquidations.

(d) If any beneficiary shall become entitled to any payment of income and/or delivery or transfer of property under the terms and provisions hereof during minority, Trustee may make such payment of income and/or delivery or transfer of property to either parent of such minor beneficiary without the necessity of guardianship proceedings on behalf of such minor beneficiary, and any payment and/or delivery or transfer so made shall relieve the Trustee of and from any and all liability by reason thereof.

(e) Upon any division or partial or final distribution of each trust estate, the said Trustee, in his sole and absolute discretion, shall have the power to partition, allot and distribute such trust estate in undivided interest or in kind, or partly in money and partly in kind, at valuations determined by the Trustee, and to sell such property as the Trustee may deem necessary, to make division or distribution, all as determined by him in the exercise of said discretion.

(f) All dividends payable in a form other than cash, and all liquidating dividends, shall be treated as principal and added to the trust estates so far as permitted by law. The determination by the Trustee as to the allocation between principal and income of any particular dividend shall be binding and conclu-

sive hereunder. The proceeds of sale of rights to subscribe for additional stock shall be treated as principal.

(g) The Trustee may receive any other property from the Donor or from any other person or persons to be held by the Trustee subject to all the terms and conditions of this trust indenture.

(h) Unless specifically limited, all discretion conferred upon the Trustee shall be absolute, and his exercise thereof conclusive on all persons interested in these trusts.

Fifth: The Trustee at any time so acting shall have the right to resign on sixty days' written notice to the beneficiaries of the trusts. In the event of such resignation, or if the Trustee is for any reason unable or unwilling to act as such Trustee, or upon the death of the Trustee, William H. Keesling shall have the right to appoint the successor Trustee.

Sixth: The trusts and each of them are hereby declared to be irrevocable, and no powers of any kind and no incidents of ownership are reserved to the Donor, and in this respect it is expressly declared to be the intent of the Donor to and he hereby does completely divest himself of all right, title and interest of every kind in these trusts and in the assets thereof. This trust indenture shall be construed under the laws of the State of California.

Seventh: The Donor hereby declares that the interest in and to the partnership doing business

under the firm name and style of Mission Company is his sole and separate property.

Eighth: The execution of this instrument by the Trustee shall be and constitute an acceptance by him of the trusts hereby created.

In Witness Whereof, the parties hereto have executed these presents at San Francisco, California, the day and year first hereinabove written.

.....,

Donor.

.....,

Trustee.

State of California,

City and County of San Francisco—ss.

On this day of, 194.., before me,, a Notary Public in and for the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Eugene Engle and John Clifton Ernst, known to me to be the persons whose names are subscribed to the within instrument and acknowledged to me that they executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal in the City and County of San Francisco the day and year in this certificate first above written.

.....,

Notary Public, in and for the City and County of San Francisco, State of California.

EXHIBIT "A"

The Mission Company
Balance Sheet

December 31, 1944

Assets

Current Assets

Cash in banks	\$ 9,726.81
Cash on hand	925.57
Inventory	15,786.58
Notes Receivable	2,000.00
Total Current Assets	<u>\$28,438.96</u>

Fixed Assets

Furniture and Fixtures	\$27,742.65
Leasehold improvements	4,360.00
Trucks and automobile	1,985.89
	<u>\$34,088.54</u>
Less: Reserve for Depreciation	7,063.74
Total Fixed Assets	<u>\$27,024.80</u>
Securities:	829.80
Cash Deposits:	2,625.00
Good Will	5,153.42
Total Assets	<u><u>\$64,071.98</u></u>

Liabilities and Capital

Liabilities:

Accounts Payable	\$ 6,761.25
Accrued Taxes	6,641.40
Notes Payable	3,319.42
Total Liabilities	<u>\$16,722.07</u>

Capital:

Umberto Dardi, Capital	\$23,674.95
Eugene J. Engle, Capital	23,674.95
Total Capital	<u>\$47,349.91</u>
Total Liabilities and Capital ...	<u><u>\$64,071.98</u></u>

EXHIBIT G

Release

For valuable consideration receipt whereof is hereby acknowledged, the undersigned, for himself, his heirs, executors, administrators and assigns, does hereby release and discharge Eugene Engle of and from any and all claims, demands, damages, liabilities, sums of money, and causes of action which the undersigned may have had or now has or hereafter may have arising out of or by virtue of that certain promissory note dated April 30, 1944, executed by said Eugene Engle to Virgil D. Dardi in the face amount of \$150,000, together with interest thereon at the rate of three per cent (3%); and the undersigned further agrees that he will cancel said note and that the same shall be of no further force and effect.

Dated: May 6, 1947.

/s/ V. DARDI.

Witnessed:

/s/ R. W. STEWART.

[Endorsed]: Filed April 11, 1957.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS
OF LAW

The above-entitled action was tried on April 15, 1957, before the court sitting without a jury, Lloyd H. Burke, Lynn J. Gillard and Joseph O. Greaves appearing for the plaintiff, United States of America, and J. Richard Johnston appearing for the defendants, The Mission Company, Virgil D. Dardi, individually and as executor of the Estate of Umberto Dardi, and Olga Paula, as trustee of trust for Joseph Dardi and as trustee of trust for Mary Claire Elevita Dardi.

Documentary evidence having been introduced and the court now being sufficiently advised and informed in the premises makes the following Findings of Fact and draws the following Conclusions of Law:

Findings of Fact

1. At all times hereinafter mentioned, the plaintiff was, and now is, a sovereign body politic.
2. This is an action arising under the laws of the United States providing for the internal revenue and the collection thereof.
3. This action has been authorized by the Attorney General of the United States at the request of the Commissioner of Internal Revenue.
4. The Mission Company is a corporation organized under the laws of the State of California and

at all times relevant to this action was doing business at 2200 Mission Street, San Francisco, California.

5. The defendants, Virgil D. Dardi and Olga Paula, are residents of San Francisco, California, or other places within the jurisdiction of this Court.

6. The Mission Company was incorporated under the laws of the State of California in January, 1941, under the name of Dardi and Company; in April, 1941, said corporate name was changed to R. J. Howell, Inc.; in November, 1942, said corporate name was changed to The Mission Company.

7. The Mission Company filed corporate income tax returns for the calendar year 1942 and for the period January 1, 1943, to June 30, 1943; said returns were filed by Virgil D. Dardi as president and Umberto Dardi as vice president.

8. Income and excess profits taxes were assessed against The Mission Company as follows:

Year	Tax	Amt. Assessed	Post War Credit	Amt. Owed
1942	E.P.	\$ 8,117.06	\$ 811.71	\$ 7,305.35
1942	I.T.	14.50		369.96
	Int.	3.47		
	DVEP	283.99		
	Int.	68.00		
1943	E.P.	6,305.04	630.50	5,674.54
1943	I.T.	726.05		2,633.75
	Int.	130.28		
	DVEP	1,507.01		
	Int.	270.41		
				<hr/> \$15,983.60

The assessment list pertaining to the above tax liabilities was signed by the Commissioner of Internal Revenue on October 10, 1947, and received by the Collector of Internal Revenue at San Francisco on October 13, 1947, on which date a lien of the plaintiff, United States of America, arose on all property and rights to property of The Mission Company; said assessment was within the applicable statute of limitations for assessment of such taxes as duly extended by Virgil D. Dardi as president of The Mission Company; notice and demand was made on The Mission Company on October 17, 1947; no part of the \$15,983.60, plus interest, due to the United States of America for the above taxes has been paid; waivers were executed by Virgil D. Dardi as president of The Mission Company on October 21, 1952, extending the time of collection of the above tax liabilities by distraint or by proceedings in court until December 31, 1956; notices of Federal tax liens were filed pursuant to Section 3672 of the Internal Revenue Code of 1939 for the tax liabilities asserted herein in the County of San Francisco, California, on January 9, 1948, in the amount of \$19,491.39.

9. No waiver extending the time of collection of the above tax liabilities by distraint or by proceedings in court has ever been executed by Virgil D. Dardi, either individually or as executor of the estate of Umberto Dardi, or by Olga Paula as trustee of the trust for Joseph Dardi or as trustee of the trust for Mary Claire Elevita Dardi.

10. On June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi each received from The Mission Company one-half of its assets and said Virgil D. Dardi and Umberto Dardi assumed the liabilities of said corporation as shown on its books at that date. On June 30, 1943, defendant Virgil D. Dardi and Umberto Dardi formed a partnership known as The Mission Co., to which they transferred the assets which they had received and the liabilities which they had assumed from the defendant The Mission Company. Said partnership thereafter continued to operate the business known as the Cigar Box Restaurant.

11. That at the time of the said transfer of all assets of The Mission Company to Virgil and Umberto Dardi, said assets had a total value as evidenced by the books of the corporation, The Mission Company, and the partnership of \$38,137.65 and that said partnership of Virgil Dardi and Umberto Dardi did assume liabilities totalling \$22,311.65.

12. On April 30, 1944, Virgil D. Dardi did transfer his one-half interest in the partnership known as The Mission Company to Eugene Engle for the sum of \$150,000 evidenced by a promissory note to be paid as follows:

\$27,900 on or before December 31, 1944;
\$30,000 on or before December 31, 1945;
\$30,000 on or before December 31, 1946;
Balance on or before December 31, 1947.

That said transaction was a bona fide transaction entered into in good faith by both parties.

13. Eugene Engle paid Virgil D. Dardi the sum of \$27,900.00 in 1944, in payment of the first installment due on said note, and Virgil D. Dardi reported the receipt of this payment in his individual Federal income tax return for the year 1944.

14. On or about January 1, 1945, Eugene Engle transferred his 50% partnership interest in The Mission Company to John Clifton Ernst, as trustee for Mary Claire Dardi and Joseph Dardi, the two minor children of Virgil D. Dardi. This transfer was evidenced by a trust indenture which was duly executed by the parties. Pursuant to this trust indenture, the trustee made payments to Virgil D. Dardi in the amounts set forth below, and Virgil D. Dardi reported the receipt of such payments in his individual Federal income tax returns for the respective years in which the payments were made:

1945	\$21,169.06
1946	\$38,175.00

15. On or about May 6, 1947, Virgil D. Dardi executed a release, discharging Eugene Engle from any further liability under his note of April 30, 1944.

16. Umberto Dardi died on or about April, 1948.

17. The defendant, Virgil D. Dardi, as executor of the Estate of Umberto Dardi, and the defendant, Olga Paula, as trustee of the trusts for Joseph and Mary Claire Elevita Dardi, are operating the Cigar Box Restaurant as partners or co-venturers.

18. The United States has withdrawn all claim against the defendant Olga Paula, as trustee of the trusts for Joseph and Mary Claire Elevita Dardi.

Conclusions of Law

1. That the Mission Company, a corporation, is liable to the United States for the amount of \$15,983.60, plus accrued interest at a rate of 6 per cent thereon from October 17, 1947, until the date of payment.

2. That the agreement of October 21, 1952, between The Mission Company and the Commissioner of Internal Revenue, extending the time for collection of the above tax liabilities, extended the time for proceeding in court against the defendant Virgil D. Dardi individually and as executor of the estate of Umberto Dardi, and this action is therefore not barred by the statute of limitations as to said Virgil D. Dardi, either individually or as executor of said estate.

3. That the transfer of the assets of The Mission Company to Virgil D. Dardi and Umberto Dardi rendered the taxpayer, The Mission Company, insolvent and unable to pay its taxes.

4. That neither Virgil D. Dardi nor Umberto Dardi paid any consideration to The Mission Company for said assets, except for the assumption of the liabilities of The Mission Company.

5. That the defendants Virgil D. Dardi and Umberto Dardi did each become liable to the United

States as transferees of The Mission Company in the amount of \$7,913.00, the net value of the assets received.

Dated: June 10, 1957.

/s/ MICHAEL J. ROCHE,
United States District Judge.

Approved as to form:

/s/ J. RICHARD JOHNSTON,
Attorney for Defendants.

Lodged May 27, 1957.

[Endorsed]: Filed June 10, 1957.

In the District Court of the United States, for the
Northern District of California, Southern Division

No. 34297

UNITED STATES OF AMERICA,
Plaintiff,

vs.

THE MISSION COMPANY, VIRGIL D. DARDI,
Individually and as Executor of the Estate of
UMBERTO DARDI; and OLGA PAULA, as
Trustee of Trust for JOSEPH DARDI and as
TRUSTEE of Trust for MARY CLAIRE
ELEVITA DARDI,
Defendants.

JUDGMENT

This cause came on to be heard on April 15, 1957, and duly submitted on May 6, 1957, it was argued by Counsel and thereupon, upon consideration thereof, it is ordered, adjudged and decreed as follows, viz.:

1. That the United States shall have judgment against Virgil D. Dardi in the amount of \$7,913.00.

2. That the United States shall have judgment against the Estate of Umberto Dardi in the amount of \$7,913.00.

3. That the United States shall have judgment against The Mission Company, a corporation, in the amount of \$15,983.60, plus accrued interest at a rate of 6 per cent thereon from October 17, 1947, until the date of payment.

4. That the United States shall have its costs.

5. That the action as to defendant Olga Paula, as trustee of the trusts of Joseph and Mary Claire Elevita Dardi, is dismissed.

Dated: June 10, 1957.

/s/ MICHAEL J. ROCHE,

United States District Judge.

Approved as to form.

/s/ J. RICHARD JOHNSTON,

Attorney for Defendants.

Lodged May 27, 1957.

[Endorsed]: Filed June 10, 1957.

Entered June 11, 1957.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given that Virgil D. Dardi, defendant above named, hereby appeals, both individually and as Executor of the Estate of Umberto Dardi, to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in the above-entitled action on June 11, 1957.

Dated: July 8, 1957.

/s/ J. RICHARD JOHNSTON,
Attorney for Said Defendant.

[Endorsed]: Filed July 10, 1957.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK TO
RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents and exhibits, listed below, are the originals filed in this Court in the above-entitled case and constitute the record on appeal herein as designated by the attorneys for the appellants:

Excerpt from Docket Entries.

Complaint.

Answer of Virgil D. Dardi, Individually.

Answer of Virgil D. Dardi, Executor Estate Umberto Dardi.

Amended Answer of Virgil D. Dardi, Individually.

Amended Answer of Virgil D. Dardi, Executor
Estate Umberto Dardi.

Pretrial order.

Motion of Defendant for Judgment on Pleadings.

Order Denying Motion for Judgment on Plead-
ings.

Stipulation of Facts with Exhibits Attached.

Findings of Fact and Conclusions of Law.

Judgment.

Stay of Judgment Pending Appeal.

Notice of Appeal.

Bond on Appeal.

Appellants' Designation of Record on Appeal.

In Witness Whereof, I have hereunto set my hand
and affixed the seal of said District Court this 1st
day of August, 1957.

[Seal]

C. W. CALBREATH,
Clerk.

By /s/ MARGARET P. BLAIR,
Deputy Clerk.

[Endorsed]: No. 15655. United States Court of
Appeals for the Ninth Circuit. Virgil D. Dardi, In-
dividually and as Executor of the Estate of Umberto
Dardi, Appellant, vs. United States of America, Ap-

appellee. Transcript of Record. Appeal From the United States District Court for the Northern District of California, Southern Division.

Filed: August 1, 1957.

Docketed: August 6, 1957.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit
No. 15655

UNITED STATES OF AMERICA,

Plaintiff,

vs.

THE MISSION COMPANY, VIRGIL D. DARDI,
Individually and as Executor of the Estate
of UMBERTO DARDI; and OLGA PAULA,
as Trustee of Trust for JOSEPH DARDI and
as Trustee of Trust for MARY CLAIRE
ELEVITA DARDI,

Defendants.

STATEMENT OF POINTS ON WHICH
APPELLANT INTENDS TO RELY

Appellant intends to rely on the following point on appeal:

The suit was barred by the statute of limitations as against all defendants except The Mission Company.

/s/ J. RICHARD JOHNSTON,
Attorney for Appellant.

Affidavit of Service by Mail attached.

[Endorsed]: Filed August 6, 1957.

No. 15,655
IN THE
United States Court of Appeals
For the Ninth Circuit

VIRGIL D. DARDI, Individually and as
Executor of the Estate of Umberto
Dardi,

Appellant,

VS.

UNITED STATES OF AMERICA,

Appellee.

On Appeal from the Judgment of the United States District Court
for the Northern District of California.

BRIEF FOR THE APPELLEE.

CHARLES K. RICE,
Assistant Attorney General.

LEE A. JACKSON,
A. F. PRESCOTT,
LOUISE FOSTER,

Attorneys, Department of Justice,
Washington 25, D.C.

LLOYD H. BURKE,
United States Attorney.

C. ELMER COLLETT,
Assistant United States Attorney.

FILED

NOV 12 1957

PAUL P O BRIEN, CLERK



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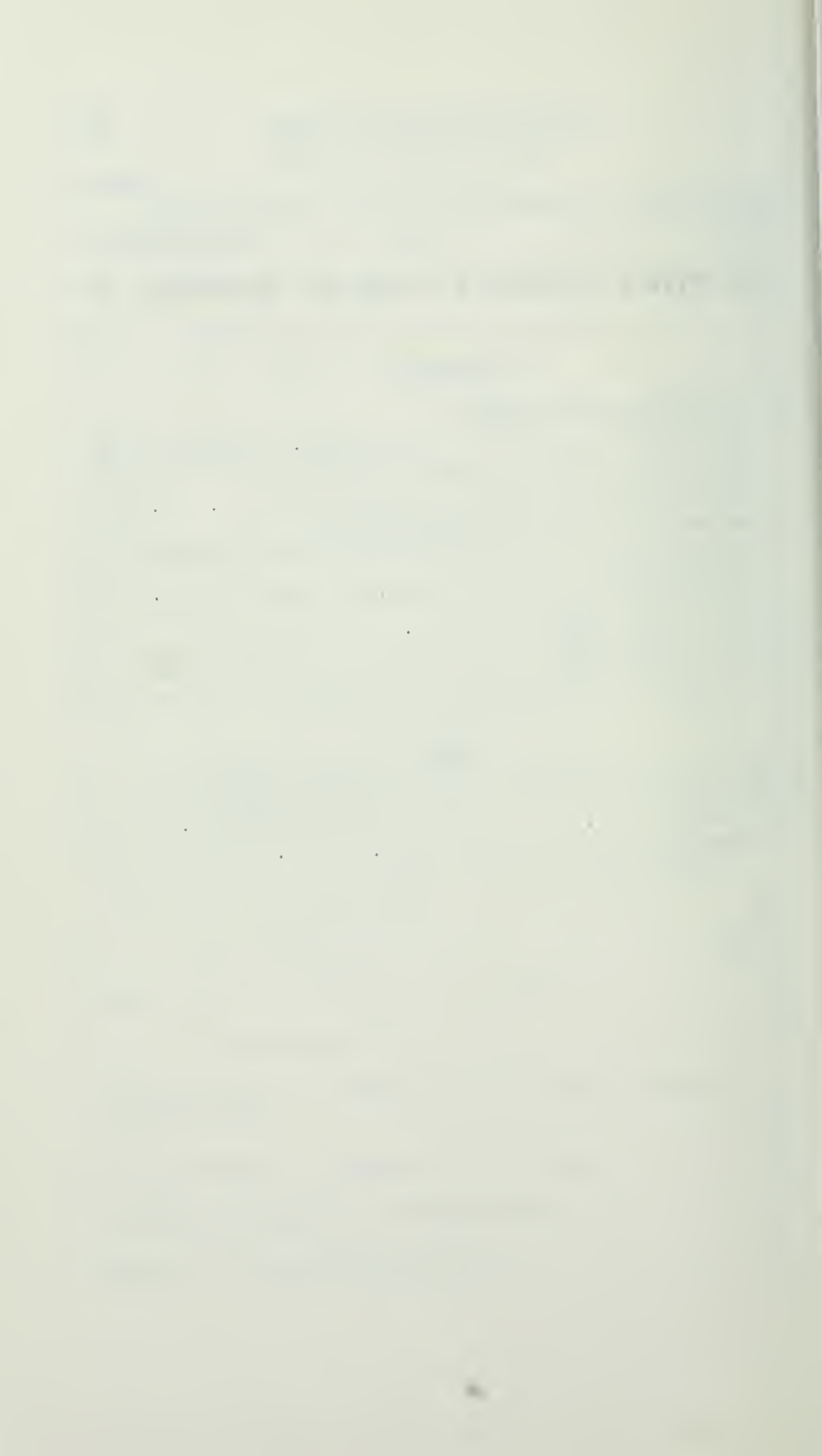
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No. 15,655

IN THE

**United States Court of Appeals
For the Ninth Circuit**

VIRGIL D. DARDI, Individually and as
Executor of the Estate of Umberto
Dardi,

Appellant,

VS.

UNITED STATES OF AMERICA,

Appellee.

On Appeal from the Judgment of the United States District Court
for the Northern District of California.

BRIEF FOR THE APPELLEE.

OPINION BELOW.

No opinion was rendered by the District Court. The findings of fact and conclusions of law appear in the record at pp. 43-49.

JURISDICTION.

This appeal involves a suit filed by the United States on December 15, 1954, in the United States District Court for the Northern District of California

to collect income and excess profits taxes assessed against the Mission Company, a corporation for the years 1942 and 1943. In addition to that company, the defendants named were Virgil D. Dardi, individually and as executor of the estate of Umberto Dardi, and Olga Paula as trustee of trusts for Joseph Dardi and Mary Claire Elevita Dardi. (R. 1-8.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1345. After filing answers, the defendants filed a motion for judgment in the pleadings on the ground that this action is barred by the statute of limitations but such motion was denied in an order entered on April 13, 1956. (R. 18-19.) After the hearing, judgment was entered on June 11, 1957 against the Mission Company and also against Virgil D. Dardi, individually and as executor. (R. 50.) The action was dismissed as to Olga Paula. (R. 50.) Notice of appeal to this Court was filed on July 8, 1957. (R. 51.) This Court has jurisdiction under 28 U.S.C., Section 1291.

QUESTION PRESENTED.

Whether this suit is barred by the statute of limitations applicable to the collection of income tax from a transferee. This depends upon whether the waiver which was executed by the appellant as president of the transferor-corporation also tolled the period of limitation for collection from the appellant in his capacity as transferee.

STATUTE INVOLVED.

Internal Revenue Code of 1939:

Sec. 276. Same—Exceptions.

* * *

(c) *Collection after assessment.*—Where the assessment of any income tax imposed by this chapter has been made within the period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court, but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer before the expiration of such six-year period. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.

(26 U.S.C. 1952 ed., Sec. 276.) * * *

Sec. 311. Transferred Assets.

(a) *Method of Collection.*—The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

(1) *Transferees.*—The liability, at law or in equity, of a transferee of property of a tax-

payer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter.

* * *

(26 U.S.C. 1952 ed., Sec. 311.)

STATEMENT.

The facts as found by the District Court are, so far as pertinent here, as follows (R. 43-48):

The Mission Company was incorporated under the laws of California in January, 1941, but used other names until November, 1942. It filed income tax returns for the calendar year 1942 and for the period from January 1, 1943, to June 30, 1943. These returns were filed by Virgil D. Dardi as president and Umberto Dardi as vice president. (R. 44.)

Income and excess profits taxes were assessed against the Mission Company as follows (R. 44):

Year	Tax	Amt. Assessed	Post War Credit	Amt. Owed
1942	E.P.	\$8,117.06	\$811.71	\$ 7,305.35
1942	I.T.	14.50		369.96
	Int.	3.47		
	DVEP	283.99		
	Int.	68.00		
1943	E.P.	6,305.04	630.50	5,674.54
1943	L.T.	726.05		2,633.75
	Int.	130.28		
	DVEP	1,507.01		
	Int.	270.41		
				<hr/> \$15,983.60

The assessment list pertaining to the above tax liabilities was signed by the Commissioner of Internal Revenue on October 10, 1947, and received by the Collector of Internal Revenue at San Francisco on October 13, 1947, on which date a lien arose on all property and rights to property of the Mission Company. This assessment was within the applicable statute of limitations for assessment of such taxes as duly extended by Virgil D. Dardi as president of the Mission Company. Notice and demand was made on the Mission Company on October 17, 1947, but none of the above taxes has been paid. (R. 45.)

Waivers which were executed by Virgil D. Dardi as president of the Mission Company on October 21, 1952, extended the time of collection of the above tax liabilities by distraint or by proceedings in court until December 31, 1956. Notices of federal tax liens were filed pursuant to Section 3672 of the Internal Revenue Code of 1939 for the tax liabilities asserted herein in the County of San Francisco, California, on January 9, 1948, in the amount of \$19,491.39. (R. 45.)

No waiver extending the time of collection of the above tax liabilities by distraint or by proceedings in court has ever been executed by Virgil D. Dardi, either individually or as executor of the estate of Umberto Dardi. (R. 45.)

On June 30, 1943, Virgil D. Dardi and Umberto Dardi each received the assets of the Mission Company and assumed the liabilities of the corporation as shown on its books at that date. On the same day they

formed a partnership known as the Mission Company, to which they transferred the assets which they had received and the liabilities which they had assumed from the Mission Company. This partnership thereafter continued to operate the business known as the Cigar Box Restaurant. (R. 46.)

At the time of the above transfer of the assets of the Mission Company, they had a total value as evidenced by the books of the corporation and of the partnership of \$38,137.65 and liabilities amounted to \$22,311.65. (R. 46.)

On April 30, 1944, Virgil D. Dardi did transfer his one-half interest in the partnership known as the Mission Company to Eugene Engle for the sum of \$150,000 evidenced by a promissory note to be paid as follows (R. 46):

\$27,900 on or before December 31, 1944;

\$30,000 on or before December 31, 1945;

\$30,000 on or before December 31, 1946;

Balance on or before December 31, 1947.

The transaction was a bona fide transaction entered into in good faith by both parties. (R. 46.)

Eugene Engle paid Virgil D. Dardi the sum of \$27,900 in 1944, in payment of the first installment due on the note, and Virgil D. Dardi reported the receipt of this payment in his individual federal income tax return for the year 1944. (R. 47.)

On or about January 1, 1945, Eugene Engle transferred his 50% partnership interest in the Mission Company to John Clifton Ernst, as trustee for Mary

Claire Dardi and Joseph Dardi, the two minor children of Virgil D. Dardi. This transfer was evidenced by a trust indenture which was duly executed by the parties. Pursuant to this trust indenture, the trustee made payments to Virgil D. Dardi in the amounts set forth below, and Virgil D. Dardi reported the receipt of such payments in his individual federal income tax returns for the respective years in which the payments were made (R. 47):

1945	\$21,169.06
1946	\$38,175.00

On or about May 6, 1947, Virgil D. Dardi executed a release, discharging Eugene Engle from any further liability under his note of April 30, 1944. (R. 47.)

Umberto Dardi died on or about April, 1948, and Virgil D. Dardi is executor of the estate of Umberto Dardi. (R. 47.)

On the basis of these facts the District Court reached the following conclusions of law (R. 48-49):

1. That the Mission Company, a corporation, is liable to the United States for the amount of \$15,983.-60, plus accrued interest at a rate of 6 per cent thereon from October 17, 1947, until the date of payment.

2. That the agreement of October 21, 1952, between the Mission Company and the Commissioner of Internal Revenue, extending the time for collection of the above tax liabilities, extended the time for proceeding in court against Virgil D. Dardi individually and as executor of the estate of Umberto Dardi, and this action is therefore not barred by the statute of

limitations as to Virgil D. Dardi, either individually or as executor of the estate.

3. That the transfer of the assets of the Mission Company to Virgil D. Dardi and Umberto Dardi rendered the taxpayer, the Mission Company, insolvent and unable to pay its taxes.

4. That neither Virgil D. Dardi nor Umberto Dardi paid any consideration to the Mission Company for the assets, except for the assumption of the liabilities of the Mission Company.

5. That Virgil D. Dardi and Umberto Dardi did each become liable to the United States as transferees of the Mission Company in the amount of \$7,913, the net value of the assets received.

Accordingly, judgment was entered by the District Court against Virgil D. Dardi as an individual in the amount of \$7,913 and against him as executor of the estate of Umberto Dardi for the same amount. Judgment was entered against the Mission Company for \$15,983.60, plus interest. (R. 50.)

SUMMARY OF ARGUMENT.

It is admitted that the taxpayer here owes taxes for 1942 and 1943, and that it became insolvent when it subsequently transferred all of its assets to its two stockholders. The only issue in this case is whether the statute of limitations bars the Government from collecting these taxes from its stockholders who are transferees within the meaning of the revenue statute.

This issue depends upon whether the waiver which was executed by the taxpayer's president to extend the time for collecting the above taxes also operates as an extension for collection from the transferees.

The statute provides that a transferee's liability for the tax of a taxpayer shall be assessed and collected in the same manner and shall be subject to the same limitations as in the case of a deficiency in tax imposed on the taxpayer. The applicable provisions as to limitations state that a tax may be collected by a proceeding in court if begun within six years after assessment or if begun within a period agreed upon by the Commissioner and the taxpayer, if such agreement is made prior to the expiration of the original six-year period. Thus, the six-year period may be extended by a waiver such as that in this case and it is conceded that the waiver here did extend the time for collecting the taxes from the taxpayer. The District Court also held that such waiver extended the time for collection from the transferees.

We submit that its decision is correct and is in accord with the rule of construction which requires statutory provisions of limitations to be strictly construed in the Government's favor. Moreover, it has long been the administrative practice to treat any waiver which stops the running of the period of limitation on assessment and collection as to the taxpayer as also suspending the period of limitations as to the transferee. Such practice has been widely approved by the courts in decisions holding that the suspension of the statute as against a transferor works a sus-

pension of the statute as to the transferees whether it is assessment or collection which is involved.

In contending otherwise, the appellant asserts that the waiver here did not extend the time as to the transferees because it was signed by him in his capacity as president of the taxpayer and not in his capacity as transferee. But his contention is not supported by the decisions which show that it is unnecessary to have waivers executed by a transferee where one has been executed by a taxpayer. The liability in both cases is, of course, for the same tax and the taxpayer's waiver stops the period of limitations from running for the time indicated therein. When the appellant here executed the waiver, he of course knew that the taxpayer had distributed all of its assets and that it no longer had anything with which to pay its taxes. Thus, he should have known that he, as a transferee, would be liable for such taxes to the extent of the assets received. At any rate, it is well established that what the appellant did when he executed the waiver for the taxpayer also extended the time for suing him as a transferee and this suit, having been commenced within the time designated in the waiver, is timely as to all of the parties, as the District Court held.

ARGUMENT.

THE DISTRICT COURT CORRECTLY HELD THAT THIS SUIT IS NOT BARRED BY THE STATUTE OF LIMITATIONS AND THAT THE TRANSFEREES ARE LIABLE, TO THE EXTENT FOUND BY THE DISTRICT COURT, FOR THE TAXES ASSESSED AGAINST THE TRANSFEROR-TAXPAYER.

There is no question here as to the liability of the Mission Company for 1942 and 1943 taxes, as found by the District Court, and no question as to the timeliness of this suit, in so far as it concerns that company. Also as the Mission Company became insolvent when it transferred all of its assets in 1944 to its two stockholders, there is now no question that these stockholders became liable, as transferees for the company's unpaid taxes for 1942 and 1943 (to the extent found by the District Court) and must pay the taxes if this suit is timely as to them. Thus, the only issue here is whether the statute of limitations bars the Government from collecting such taxes from the transferees.

Of course, by the time this suit was filed on December 15, 1954 (R. 8), Umberto Dardi, one of the transferees, had died. However, his son Virgil, who is the other transferee, became executor of his father's estate and entered an appearance not only in his individual capacity but also as executor of that estate. (R. 9-13.) Virgil has also been president of the Mission Company and in that capacity executed a waiver on October 21, 1952, extending the period for collection of the company's taxes, either by distraint or by proceeding in court, until December 31, 1956. (R. 45.) In view of such waiver (admitted by appellant to be effective as to the company) the issue here depends

upon whether the waiver is effective to extend the time for collecting these taxes from the transferees. The District Court held (R. 48) that the waiver did extend the time for suing the transferees and therefore concluded that this suit was not barred by the statute of limitations. We submit that the District Court's decision is correct.

Section 311(a) of the 1939 Internal Revenue Code, *supra*, provides that a transferee's liability for the tax of a taxpayer from whom he has received property shall be assessed and collected in the same manner and shall be *subject to the same provisions and limitations* as in the case of a deficiency in tax imposed on the taxpayer. To determine the limitations on collection from a transferee, we must turn to the 1939 Code, Section 276(c), *supra*, which provides that where the assessment of any income tax has been made within the period of limitation applicable thereto,¹ such tax may be collected by a proceeding in court if begun within six years after the assessment of the tax or may be so collected if such suit is begun prior to the expiration of any period for collection which is agreed upon in writing by the Commissioner and the taxpayer before the original six-year period expires. Section 276(c) also provides that the period so agreed upon

¹While the record does not set out full details as to what transpired between the time that the tax returns of The Mission Company were filed and its taxes were assessed on October 13, 1947 (R. 44-45), the parties have accepted that assessment as timely. Consequently, there is no question here as to the assessment and our discussion will be confined to the statutory provisions relating to collection.

may be extended by subsequent agreements in writing made before the first period expires.

In other words, the six-year period for commencing a suit to collect taxes may be extended by executing a waiver which has the effect of extending the time until the date named therein; and that is exactly what was done here. As we have indicated, the appellant not only admits (Br. 6) that there was such a waiver here but he also admits that it did extend the time in which a collection suit could be filed against the taxpayer-corporation, and that this suit is timely as to that company. But the appellant contends that the waiver is not effective as to him either in his individual capacity or as executor of his father's estate because he signed the waiver as president of the taxpayer-corporation and not as a transferee. The appellant's contention is squarely in conflict with *United States v. City of New York*, 134 F. Supp. 374 (S.D. N.Y.) on which the District Court relied. (R. 19.)

In the *City of New York* case, a waiver extending the time for collecting unpaid taxes had been executed by the taxpayer and suit was subsequently brought against the transferees but within the period designated by the waiver. As here, the transferees in that case argued that the waiver there did not toll the period of limitation as to them because such waiver had been executed by the taxpayer. But in holding that the suit was timely as to the transferees, the Court in that case said (pp. 377-378):

The waiver of the limitation period contemplated by subdivision (2) of § 276(c) is intended for the benefit of the taxpayer; and in the event of favorable action upon his compromise offer resulting in a reduction of tax, the benefit thereof also inures to the taxpayer's transferee,—to the extent that the Government's potential claim against the transferee is also reduced. Nothing contained in the statute indicates that Congress intended, where a taxpayer consented to extend the limitation period in seeking favorable action upon his offer of compromise, that the Government's time to proceed as against the taxpayer's transferee would be running against it while the matter was under consideration; that the six year rather than the extended period controlled. *Such an interpretation would lead to unwarranted results. It would mean that in extending a benefit to the taxpayer the public fisc would be at a disadvantage in its efforts to pursue assets in the hands of a transferee.* Such an interpretation also would go counter to the settled principle of public policy that "Statutes of Limitation barring the collection of taxes must receive a strict construction in favor of the Government. Limitation will not be presumed in the absence of clear congressional action." (Italics supplied.)

We submit that the above excerpt gives the correct interpretation of the applicable statutory provisions and was properly followed by the District Court here. This is not a novel view but has long been the interpretation given in such cases, and is obviously a logical one. The question of whether a transferor by extend-

ing the time by which suit for collection may be brought against him also extends the time for collecting from the transferee involves the construction of the limitations statute. That construction is one which will apply to all cases regardless of the particular facts involved. The liability of a transferee is secondary rather than primary, and excepting where it is shown that it would prove an idle gesture, the Government must first exhaust all remedies against the taxpayer-transferor before holding the transferee liable. *Commissioner v. Oswego Falls Corp.*, 71 F. 2d 673, 676 (C.A. 2d), *Swan Land and Cattle Co. v. Frank*, 148 U.S. 603. Hence it is clear that the appellant's contention here would render useless the very purpose for which Congress has authorized waivers for extending the statute of limitations; and such a construction would prove detrimental to a transferor and to his transferee as well as disadvantageous to the Government. But as the court said in the *City of New York* case (p. 378)—

Absent congressional enactment the collection of taxes by the Government is subject to no time limit. Congress was not required to fix any period of limitation. In fixing a period of repose and in authorizing its extension upon an agreement by the taxpayer it had the clear right to provide that the extended period shall bind both the taxpayer and his transferees.

In contending that the *City of New York* case is based upon a misunderstanding of the law, the appellant objects (Br. 11) particularly to the statement in

the above excerpt that the statute of limitations are to be strictly construed in favor of the Government and asserts that such statement is contrary to the well settled law but as the decisions of this Court and of other courts show it is the appellant who is in error. Some years ago this Court stated in *Pacific Coast Steel Co. v. McLaughlin*, 61 F. 2d 73 affirmed, 288 U.S. 426, that the statute of limitations barring collection of taxes which are due and unpaid must receive a strict construction in favor of the Government and that limitations will not be presumed in absence of clear Congressional action. Subsequently that principle was reiterated by this Court in *McCarthy Co. v. Commissioner*, 80 F. 2d 618, a case involving a waiver extending the time for assessment. The same principle was approved in *Du Pont de Nemours & Co. v. Davis*, 264 U.S. 456, 462, and in *Loewer Realty Co. v. Anderson*, 31 F. 2d 268 (C.A. 2d), certiorari denied, 280 U.S. 558. In arguing against this principle, the appellant cites (Br. 11) *Bowers v. N.Y. & Albany Co.*, 273 U.S. 346, which was decided several years before the *McCarthy* case and is not actually in conflict with it. While the *Bowers* case (which involved a collection by distraint) recognized the rule quoted in the *City of New York* case, it also indicated that tax laws are to be interpreted liberally in favor of the taxpayers. But since deciding the *Bowers* case, the Supreme Court has been active in stopping attacks based on the statute of limitations which have been made following its ambiguous statement in that case. This was pointed out in Section 57.02 of 10 Mertens, Law of

Federal Income Taxation (1948) where it was stated that the rule we refer to has been scrupulously adhered to in the large majority of cases.²

But as we have indicated, there is more to support the District Court's decision here than the rule of construction we have referred to. Indeed, it has long been the administrative practice to consider anything which stops the running of the period of limitation on assessment of the taxpayer and on collection from him (whether by waiver or by specific statutory provision on limitation) as also stopping the running of the period of limitation against the taxpayer's transferee. And such practice has been approved by this and other courts in many cases. This was clearly indicated in *First Nat. Bank of Chicago v. Commissioner*, 112 F. 2d 260 (C.A. 7th), certiorari denied, 311 U.S. 691, where it was said (p. 261):

We agree with the reasoning of these cases and in the conclusion that suspension of the statute as against the transferor works a suspension of the statute as to the transferees, and, as held in

²In indicating his approval of the above rule, Mertens states (*supra*, p. 164):

In perhaps no other single phase of the income tax acts would a tendency to favor the taxpayer involve inherently such dangerous potential consequences to the public treasury. Errors of administration in the early years and attempts by Congress to overcome the effects of court decisions or to legislate the answer in later acts to problems arising under earlier acts have created questions of startling proportion in terms of the amounts involved. The Supreme Court has been active in stopping attacks predicated on the statute of limitations following its early decision in the *New York & Albany Lighterage* case [273 U.S. 346]. Recently there has been a noticeable tendency in many of the cases to cut through the technical issues involved and to rely upon the doctrine of estoppel.

the *Sanborn* case, that the suspension of the statute as to liability asserted against the executors works likewise a suspension of the statute as to the transferees. * * *

In reaching that conclusion the Seventh Circuit cited similar decisions by the Court of Claims and three other Courts of Appeals including this Court's decisions in *Commissioner v. Gerard*, 78 F. 2d 485, and *California Iron Yards Corp. v. Commissioner*, 82 F. 2d 776, certiorari denied, 299 U.S. 553. The Tax Court has also long been of the same opinion. See *Gatto v. Commissioner*, 20 T.C. 830; *Rite-Way Products v. Commissioner*, 12 T.C. 475; and *Menger v. Commissioner*, 17 B.T.A. 998.

As appellant argues here (Br. 13-14) that there are significant differences between the statutory provisions relating to assessment and those relating to collection and that these differences support his contention, we call attention to the waiver which was filed by the taxpayer-corporation in the *Rite-Way* case. As to this, the Tax Court said (pp. 478-479):

The petitioners concede * * * that the period of limitations for assessment and collection against *Rite-Way* was extended by proper consents filed by *Rite-Way*. It is also clear that the liquidating distributions were complete and thereafter *Rite-Way* was without any funds with which to pay the deficiencies and interest. The petitioners contend, nevertheless, that the period of limitations for assessment against and collection from the transferees expired within one year after the expiration of the original period of limitations

with respect to the taxpayer; that is, that the consents had no effect in so far as the transferees are concerned. *This question was decided long ago against the petitioners.* The statute provides that the period of limitations for assessment of the transferee liability in the case of initial transferees of the property of the taxpayer shall be within one year after the expiration of the period of limitations for assessment against the taxpayer. Sec. 311 (b) (1). *That means the original period of limitation for assessment against the taxpayer as properly extended by consents.* * * * (Italics supplied.)

Thus, it will be seen that the statute of limitations was suspended there by a waiver or consent executed by the taxpayer-corporation and that the Tax Court held that such waiver did extend the time for assessing the transferees. In other words, the time for assessing the transferees was not one year beyond the original period, as the transferees argued there, but one year beyond the original period as extended by the taxpayer's waiver. We submit that the same principle is applicable to waivers which are executed, as in this case, by the taxpayer to extend the time for collection of the tax.

Consequently, the appellant is in error in asserting (Br. 13) that the *City of New York* case (on which the District Court relied here) is "based upon an unsound analogy between action extending the time for *assessment* of tax and agreements extending the period for *collection*." What the appellant appears to be referring to is the provision in the 1939 Code,

Section 272, which prohibits the Commissioner from making an assessment for a designated time after a notice of deficiency is mailed to the taxpayer and a petition for redetermination is filed with the Tax Court. It is true that such procedure automatically postpones any assessment against a transferee but it is also obvious that it extends the time for collection as well, and it is not material that Section 272 does not state that collection will be affected by such action. The important thing to note here is that a taxpayer is authorized by Section 276 to execute waivers and that these may postpone the time for collection as well as for assessment. Furthermore, such waivers are equally effective as to the taxpayer's transferee.

That this is so was clearly indicated in *Lucas v. Hunt*, 45 F. 2d 781. (C.A. 5th). There a waiver was signed by Hunt as the president of the taxpayer-corporation. The waiver was slightly more than three years after the corporation was dissolved and after its assets had been transferred to Hunt and others. The Commissioner assessed Hunt as transferee within the period designated in the waiver and the latter contended that assessment was barred by the statute of limitations. Among the arguments advanced by Hunt was the one that the waiver was not valid since under Texas law he had no authority to act for the dissolved corporation when the waiver was executed. But the Fifth Circuit held otherwise, stating that (p. 782):

We are of opinion that Hunt by signing the waiver estopped himself to question its validity,

with the result that he was bound to respond to the assessment to the extent of funds in his hands which belonged to the dissolved corporation taxpayer. * * *

The waiver was executed before the assessment was barred; without it the commissioner in the performance of his duty would have made the assessment within the statutory period. The very purpose he had in mind in requiring an extension of time was to make an assessment after the statutory period of limitation had run. * * *

The same conclusion was also reached in *Benoit v. Commissioner*, 238 F. 2d 485 (C.A. 1st); *Lloyd v. Commissioner*, 29 B.T.A. 74. Also cf. *Stearns Co. v. United States*, 291 U.S. 54, 61.

We submit that the Government's position is even stronger than it was in the *Hunt* case for the appellant here does not argue that he had no authority to execute the waiver on behalf of the taxpayer-corporation. Instead, appellant admits (Br. 6) that the waiver is effective as to his company and so concedes its validity.³ But appellant objects to the waiver because it made no reference to any transferee, and because he did not execute it in his individual capacity or as executor of his father's estate. In this connection he states that he had no reason to suppose that he was

³In view of this concession, we think it is unnecessary to discuss California law as to corporations in the process of dissolution. However, in view of this Court's statement as to the California corporation law in *A B C Brewing Corp. v. Commissioner*, 224 F. 2d 483, and in *California Iron Yards Corp. v. Commissioner*, *supra*, we think it is evident that the appellant as president of the Mission Company could take any step necessary in discharging such obligations as taxes and did have authority to execute the waiver.

extending the time against himself individually or as executor and explains that "if he considered the matter at all he could reasonably have concluded that the Government intended to look only to the corporation for the payment of the taxes in question". (Br. 7.) It seems incredible that appellant would make such an assertion for he was in a position to know the facts when he signed the waiver and the facts are that he and his father had already distributed all of the assets to themselves and their corporation had nothing with which to pay its taxes. Under these circumstances, it must have been obvious to the appellant that he and his father would be held liable as transferees. At any rate it is well established that waivers like the one here do stop the running of the period of limitations not only as to the taxpayer but also as to its transferees.

Appellant's position is obviously different from that of the person who executed the waiver in *Commissioner v. Bryson*, 79 F. 2d 397 (C.A. 9th), on which appellant relies. (Br. 8.) The waiver in that case was signed by a former secretary of the taxpayer-corporation. Such waiver was also accompanied by a letter from an attorney explaining that the former officers could not legally act for the corporation which had been out of business for about five years and that the former secretary who signed the waiver was not acting as the actual secretary. This Court held that the waiver in that case was a nullity both as to the corporation and as to the transferees. In reaching its conclusion, this Court said (p. 401):

When the respondent informed the Commissioner that he would not presume to act for the corporation, when the document was signed only by a "former officer," and when it failed to bear the corporate seal, the Commissioner, as a reasonable man, should have been put on notice that, both in fact and in law, he had before him an abortive paper, binding neither corporation nor individual.

Since the waiver of 1924 was a nullity, the period of limitations ran in favor of the corporation, and therefore in favor of the respondent as alleged transferee.

Appellant also refers (Br. 12) to *United States v. Markowitz*, 34 F. Supp. 827 (N.D. Calif.), which was cited in the *City of New York* case with approval. As the appellant indicates, the waiver there was executed by the transferee and in that respect differs from the facts here. However, the *Markowitz* case contains an excellent statement of the general principle applicable here. In that case, the transferee signed two waivers but argued that no effect could be given to the second one because it was executed after the time allowed by the statute, i.e., six years after the assessment of the tax. But in holding that both waivers were timely, the court there pointed out that the provisions of Section 276(c) apply to a transferee as well as to a taxpayer and stated that we may not assume that Congress intended to create a shorter statutory period for the commencement of an action against the transferee than is provided for the commencement of the action against the taxpayer himself. We submit that

is a correct statement of the law applicable here. The tax liability which is imposed on the transferee is the same as that imposed on the taxpayer and when the latter acts through its officers to extend the period for assessment and collection of such tax, such waiver stops the running of the statute of limitations as to the transferee as well as for the taxpayer.

CONCLUSION.

The decision of the District Court is correct and should be affirmed.

Respectfully submitted,

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November, 1957.

No. 15,655

IN THE

United States Court of Appeals
For the Ninth Circuit

VIRGIL D. DARDI, Individually and as
Executor of the Estate of Umberto
Dardi,

Appellant,

VS.

UNITED STATES OF AMERICA,

Appellee.

BRIEF FOR APPELLANT.

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FILED

OCT 10 1957



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No. 15,655

IN THE

**United States Court of Appeals
For the Ninth Circuit**

VIRGIL D. DARDI, Individually and as
Executor of the Estate of Umberto
Dardi,

Appellant,

VS.

UNITED STATES OF AMERICA,

Appellee.

BRIEF FOR APPELLANT.

STATEMENT OF JURISDICTION.

This appeal involves a suit commenced by the United States on December 15, 1954, in the United States District Court for the Northern District of California. The suit was brought against The Mission Company, a corporation; the appellant, Virgil D. Dardi, both individually and as Executor of the Estate of Umberto Dardi; and Olga Paula, as trustee of trusts for Joseph Dardi and Mary Claire Elevita Dardi. The District Court had jurisdiction under 28 U.S.C., Sections 1331 and 1340. Judgment was entered on June 11, 1957, against The Mission Company and against appellant, both individually and as executor. (R. 50.) The action was dismissed as to the defend-

ant Olga Paula, trustee. (*Ibid.*) Notice of appeal to this Court was filed on July 10, 1957. (R. 51.) The appeal was timely. (Rule 73(a), Federal Rules of Civil Procedure.) This Court has jurisdiction to review the final judgment of the District Court. (28 U.S.C., Sections 1291, 1294.)

STATEMENT OF THE CASE.

This is a suit brought by the government to collect income and excess profits taxes assessed against one of the defendants, The Mission Company, a California corporation, for the years 1942 and 1943. The other defendants, including appellant, were sued as transferees. There is no dispute as to the facts of the case, which are set forth in a pre-trial order (R. 13) and a stipulation of facts. (R. 20.) The Mission Company is a California corporation which operated a restaurant in San Francisco, California, in 1942 and part of 1943. Virgil D. Dardi, the appellant, was the president of the corporation at that time, and his father, Umberto Dardi, since deceased, was the vice-president. On June 30, 1944, the corporation transferred all of its assets to the two Dardis and they assumed all of the corporation's liabilities. On the same day, these two individuals formed a partnership to carry on the restaurant business, and they transferred all of the assets and liabilities to the partnership, which continued to operate the business.

Virgil D. Dardi subsequently transferred his one-half interest in the partnership to one Eugene Engle,

and Engle later transferred this interest to trusts for the two minor children of Dardi.

The taxes in question, which amount to \$15,983.60, were assessed against the corporation on October 10, 1947. No assessment was ever made against appellant. On October 21, 1952, appellant, as president of The Mission Company, signed waivers extending until December 31, 1956, the time of collection of the taxes in question by distraint or by proceedings in Court. However, appellant signed no such waiver in his individual capacity or as Executor of the Estate of Umberto Dardi. This suit was commenced in the District Court on December 15, 1954, and Dardi was joined as a defendant, both individually and as executor of his father's estate.

On March 6, 1956, the District Court issued a pre-trial order (R. 13), and on March 28, 1956, appellant filed a motion for judgment on the pleadings (R. 18) on the ground that the action was barred by the statute of limitations, since it was commenced more than six years after the right of action accrued and appellant did not agree to any extension of the applicable period of limitation. On April 13, 1956, the Honorable O. D. Hamlin, United States District Judge, issued the following order denying the motion (R. 19):

“Upon the authority of the case of *United States v. City of New York, et al.*, S.D.N.Y., 134 F. Supp. 374, the reasoning of which case appears to the Court to be sound, it is hereby ordered that the motion of the defendant for judgment on the pleadings be, and the same hereby is, denied.”

The parties then entered into a written stipulation of facts (R. 20), and the case was submitted to the Honorable Michael J. Roche, United States District Judge, without the introduction of further evidence. Judgment, which was entered on June 11, 1957, (R. 50) was against The Mission Company in the amount of \$15,983.60, against appellant individually in the amount of \$7,913.00, and against the Estate of Umberto Dardi in the amount of \$7,913.00.

SPECIFICATION OF ERROR.

1. The judgment against appellant was based upon the following erroneous conclusion of law (R. 48):

“2. That the agreement of October 21, 1952, between The Mission Company and the Commissioner of Internal Revenue, extending the time for collection of the above tax liabilities, extended the time for proceeding in court against the defendant Virgil D. Dardi individually and as executor of the estate of Umberto Dardi, and this action is therefore not barred by the statute of limitations as to said Virgil D. Dardi, either individually or as executor of said estate.”

This conclusion is erroneous in that said agreement extending the time for collection of the tax in question did not purport to extend and did not extend the time for proceeding against appellant, either individually or as executor of the estate of Umberto Dardi, and this suit was therefore barred as to appellant under Section 276(c) of the Internal Revenue Code of

1939 (26 U.S.C., Section 276(c)) on October 10, 1953, six years after the taxes were assessed against the corporation.

ARGUMENT.

- I. THIS SUIT WAS BARRED, AS TO APPELLANT, UNDER SECTION 276(c), INTERNAL REVENUE CODE OF 1939, IN THE ABSENCE OF AN EFFECTIVE AGREEMENT IN WRITING EXTENDING THE TIME FOR SUIT.**

Section 276(c) of the Internal Revenue Code of 1939 (26 U.S.C., Sec. 276(c)) provides as follows:

“(c) Collection after Assessment.—Where the assessment of any income tax imposed by this chapter has been made within the period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court, but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer before the expiration of such six-year period. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.”

A parallel provision was enacted as Section 6502(a) of the Internal Revenue Code of 1954 (26 U.S.C., Sec. 6502(a)).

The taxes here in question were assessed against The Mission Company on October 10, 1947 (Pre-Trial Order, R. 15), and the suit was not commenced until December 15, 1954 (Complaint, R. 3 to 8). The suit was therefore barred on October 10, 1953, unless the

period had previously been extended by an effective agreement in writing.

II. THE PERIOD FOR SUIT AGAINST APPELLANT WAS NOT EXTENDED BY THE AGREEMENT BETWEEN THE COMMISSIONER AND THE MISSION COMPANY.

A. Section 276(c) does not so provide.

There is no question but what an effective agreement was entered into between the Commissioner and The Mission Company, and that the period for suit was effectively extended as to that defendant. However, no such agreement was ever executed by the appellant individually or as executor of the Estate of Umberto Dardi (Pre-Trial Order, R. 16), and the suit was therefore barred as to him unless the agreement executed by The Mission Company had the effect of extending the time for suit against appellant, as well as against that corporation.

Section 276(c) warrants no such conclusion. The section makes no specific reference to suits against transferees. While it does provide generally that the time for suit may be extended by an agreement in writing between the Commissioner and "the taxpayer", the term "the taxpayer" has been held to refer to a transferee as well as to the original taxpayer.

United States v. Updike (1930), 281 U.S. 489, 494, 50 S.Ct. 367, 368-369;

United States v. Markowitz (N.D. Cal. 1940), 34 F. Supp. 827, 830.

These cases make it clear that the six year period of limitations under Section 276(c) applies to a suit against a transferee, and that the period may be extended by an agreement signed *by the transferee*. *They provide no basis for concluding that the period for suit against the transferee may be extended by an agreement signed only by anyone else.*

On the contrary, Section 276(c) should be construed to mean that the period may be extended as to the original taxpayer by an agreement signed by him, and as to a transferee by an agreement signed by him, and no more. There is nothing in the section to warrant the conclusion that the period for suit against the one may be extended by an agreement signed by the other.

B. Appellant should not be bound by an agreement to which he was not a party.

While the agreement extending the time for suit against The Mission Company was signed by appellant as president of that corporation (Pre-Trial Order, R. 15), it made no reference to any transferee, nor was appellant a party to the agreement in his individual capacity or as executor of his father's estate (Pre-Trial Order, R. 16). Not only had he no reason to suppose that he was extending the time for a possible suit against him individually or as executor, but if he considered the matter at all he could reasonably have concluded that the Government intended to look only to the corporation for the payment of the taxes in question. Had the Government intended to extend the period for suit against appellant, it could easily

have indicated its intention by requesting a similar agreement from him, or at least by mentioning him in the agreement which appellant signed as president of the corporate taxpayer. It did neither.

In *Commissioner v. Bryson* (C.A. 9, 1935), 79 F. 2d 397, this Court considered the effect of a waiver of the statutory period of limitations for assessment and collection of corporate income tax, signed by a transferee as "former secretary" of a corporate taxpayer. It was held that the waiver was binding neither on the corporation nor on the transferee individually. In the Court's majority opinion, written by Judge Garrecht, it is stated:

"... Neither the purported waiver nor the accompanying letter contains any statement that the respondent was the transferee of the Corporation. Without distorting plain words from their ordinary meaning, a transferee's waiver cannot be spelled out of the inchoate paper that we are here considering."

79 F. 2d at p. 401.

In his concurring opinion, Judge Denman stated the point even more forcefully:

"... Had the Commissioner of Internal Revenue sought a waiver of the statute of limitations by Bryson individually, it would have been simple enough to make plain that intention without varying from the general form of 'Income and Profits Tax Waiver' which has been in customary use in the Internal Revenue Department since the Revenue Act of 1921, and which was the form utilized

in the instant case. Bryson might have been named in the body of the instrument as 'transferee.' A description of him there as 'taxpayer' would have been amply sufficient. It is a persuasive factor negating the Commissioner's intent to hold Bryson personally, that instead of taking such elementary steps to cause the waiver to speak thus clearly, he affixed his signature to a document which on its face bound no one, and from which can be read a transferee liability only by an ultra refined metaphysical construction animated by a strong presumption in favor of the government and against the taxpayer. In addition to the proper presumption which is against the government it may be said that if there were doubt as to the interpretation of the terms of the writing, that doubt certainly should not be resolved with any presumption in favor of the party furnishing the printed form."

Ordinarily, action by one joint debtor which suspends the running of the statute of limitations does not remove the bar of the statute as to his codebtor, and there would seem to be no particular reason why a contrary rule should be applied in the circumstances of this case.

"An acknowledgement by a joint debtor does not remove the bar of the statute as to his codebtor. The promise of one of several joint debtors cannot avail to revive as against the others a cause of action barred by the statute, or to suspend the running of the statute."

1 Wood on Limitations (1916), Sec. 81d(2), pp. 440-441.

“It is an established general rule that in order to take a case out of the statute of limitations, an acknowledgment or new promise must be made by someone legally authorized by him so to act, such as his duly authorized agent or attorney.”

34 Am. Jur., Limitations of Actions, Sec. 327, p. 258.

If the government desired to extend the time for suit against appellant as a transferee, it should have asked him to sign an agreement in his individual capacity, or as executor of Umberto Dardi's estate. At the very least it could have indicated in the agreement signed by appellant on behalf of the corporation that it was thereby intended to extend the time for suit against transferees as well as against the corporate taxpayer. Having failed to follow either of these courses of action, the government should not now succeed in its argument that the execution of the agreement by the corporation had the effect of extending the time for suit against appellant as a transferee.

C. The case of *United States v. City of New York* was incorrectly decided and should not be followed.

Appellant's motion for judgment on the pleadings in the District Court was denied solely upon the authority of *United States v. City of New York, et al.* (S.D. N.Y., 1955), 134 F. Supp. 374. This appears to be the only reported decision which is squarely on the issue here presented.

In *City of New York* a taxpayer had made an offer in compromise which contained a customary provision

agreeing to a suspension of the running of the statutory period of limitation on collection of the tax sought to be compromised during the period the offer was under consideration and for one year thereafter. Judge Weinfeld, a district judge, held that this action by the taxpayer also tolled the period of limitation as against his initial transferees. Appellant believes that the case was incorrectly decided, for the following reasons:

(1) The decision is expressly based upon a misconceived theory, stated by the Court as follows:

“Statutes of limitation barring the collection of taxes must receive a strict construction in favor of the government. Limitation will not be presumed in the absence of clear congressional action.”

The well-settled law is precisely the opposite: such statutes are to be construed liberally in favor of the taxpayer.

In *Bowers v. New York & Albany Company* (1927), 273 U.S. 346, 47 S.Ct. 389, the Supreme Court held that a statute barring any “suit or proceeding” for the collection of taxes five years after the return was filed should be construed to bar collection by distraint as well as by Court action. The Court said:

“The limitation applies to petitioner and to the claims. It applies to suit; the only question is whether it also bars distraint. The provision is a part of a taxing statute; and *such laws are to be interpreted liberally in favor of the taxpayers.*” (Emphasis added.)

273 U. S. at p. 349, 47 S.Ct. at p. 390.

In *United States v. Updike* (1930), 281 U.S. 489, 50 S.Ct. 367, the Supreme Court referred to "the rule which requires taxing acts, including provisions of limitation embodied therein, to be construed liberally in favor of the taxpayer." (281 U.S. at p. 496, 50 S.Ct. at p. 369.) The Court cited the *Bowers* case, *supra*.

In *Commissioner v. Bryson* (C.A. 9, 1935), 79 F. 2d 397, this Court, citing *Updike*, said:

"It is familiar doctrine that 'taxing acts, including provisions of limitation embodied therein [are] to be construed liberally in favor of the taxpayer.' "

79 F. 2d at p. 402.

(2) The decision in *City of New York* is based upon a misunderstanding of Section 311, Internal Revenue Code of 1939, and a misinterpretation of the opinion of the District Court for the Northern District of California in *United States v. Markowitz* (N.D. Cal. 1940), 34 F. Supp. 827. In footnote 11 to its opinion in *City of New York* the Court quotes language from the *Markowitz* opinion which, taken out of context, might seem to mean that the government could proceed against the transferee as long as the period remained open against the original taxpayer. However, in *Markowitz* the fact was that the *defendant transferee himself* had signed a waiver extending the period of limitations, and the Court held that this agreement was effective in extending the period for suit against the transferee. What the Court was

really saying in that portion of its opinion quoted in *City of New York* was that the period for proceeding against the transferee could be extended by his agreement, just as the period for proceeding against the original taxpayer could be extended by *his* agreement. In this sense, the same period is applicable to both, *viz.* six years plus any extension agreed to by the party proceeded against.

(3) The decision in *City of New York* is based upon an unsound analogy between action extending the time for *assessment* of tax and agreements extending the period for *collection*. Judge Weinfeld points out that the period for assessment of tax against a transferee may be extended by the action of the taxpayer-transferor in filing a petition with the Tax Court or executing an agreement extending the limitation period, and argues that this situation is analogous. (134 F. Supp. at p. 378.)

The difference, however, is that the period of limitation for *assessment* of tax against a transferee is determined, by express statutory provision, by the period for assessment against the original taxpayer. Section 311(b)(1) and (2) provides as follows:

“(1) In the case of the liability of an initial transferee of the property of the taxpayer,—within one year after the expiration of the period of limitation for assessment against the taxpayer;

(2) In the case of the liability of a transferee of a transferee of the property of the taxpayer,—within one year after the expiration of the period of limitation for assessment against the preced-

ing transferee, but only if within three years after the expiration of the period of limitation for assessment against the taxpayer;—”

Obviously, any extension of the period for assessment against the transferor-taxpayer automatically extends the period for assessment against his transferee.

There is no parallel provision in the Code regarding the extension of time for *collection*, as distinguished from *assessment*. If Congress had intended a similar rule to apply to collection, it would presumably have said so. The fact that no such rule was incorporated in the Code indicates that none was intended to apply.

Moreover, the reasons which underlie the statutory rule with regard to assessment are not applicable to the matter of collection. An extension of time for assessment benefits transferor and transferee alike, since it gives the government additional time to determine the correct amount of the tax liability. All parties affected have the advantage of that time to present evidence and argument as to the amount of the liability. However, after the assessment is made and all that remains is to collect the tax, an extension of the period of limitation which is desired by the transferor-taxpayer may be of no benefit whatsoever to the transferee. Indeed, to the extent that he is misled into believing that no action is contemplated against him, it may be positively detrimental.

In the *New York City* case the agreement extending the time for collection was incorporated in an offer in compromise made by the transferor-taxpayer.

Judge Weinfeld argues that this agreement might have benefited the transferee as well as the transferor-taxpayer, since the government might have acted favorably on the offer and thereby reduced its potential claim against the transferee. The present case differs, however, in that no offer in compromise was involved and there is no evidence that any reduction in the amount of the assessment was ever considered.

In short, the case of *United States v. City of New York, et al.* was incorrectly decided and should not be followed.

CONCLUSION.

The judgment against appellant, both individually and as Executor of the Estate of Umberto Dardi, should be reversed and judgment entered in favor of appellant.

Dated, Oakland, California,
October 7, 1957.

Respectfully submitted,

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By J. RICHARD JOHNSTON,

Attorneys for Appellant.

No. 15,655

IN THE

United States Court of Appeals
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UNITED STATES OF AMERICA,

Appellee.

REPLY BRIEF FOR APPELLANT.

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UNITED STATES OF AMERICA,

Appellee.

REPLY BRIEF FOR APPELLANT.

SUMMARY OF ARGUMENT.

The only issue presented in this case is whether a waiver executed by a transferor taxpayer, extending the normal six-year period for collection of tax after assessment, extends the period for collection proceedings against a transferee. In considering this issue a clear distinction must be made between extensions of the period for assessment of tax and extensions of the period for collection proceedings after assessment.

The attempted analogy between extensions of the period for assessment and extensions of the period for collection after assessment is not valid, and cases in-

volving the former period do not support the District Court's decision in this case, which involves only the latter period. The issue of this case has been considered in only one reported decision, *United States v. City of New York* (S.D. N.Y., 1955), 134 F. Supp. 374. The case was incorrectly decided and should not be followed.

There is, moreover, no evidence of any established administrative practice, as alleged by appellee, which supports the Government's position in this case. None of the cases cited by the appellee as evidence of such a practice relates to the issue presented in this case, and the case of *United States v. Markowitz* (N.D. Cal., 1940), 34 F. Supp. 827, may well indicate a contrary practice.

The rule that statutes of limitation barring the collection of taxes should be liberally construed in favor of the taxpayer, which has been acknowledged by the Supreme Court and by this Court, still stands, and it has not been changed by any decisions subsequent to those upon which we rely.

ARGUMENT.

I. THE ISSUE PRESENTED IN THIS CASE RELATES ONLY TO THE PERIOD FOR COLLECTION, AND NOT TO THE PERIOD FOR ASSESSMENT OF TAX.

This appeal presents but one issue: When the transferor taxpayer, The Mission Company, executed a waiver extending the normal six-year period for collection of the tax previously assessed against that tax-

payer, did it thereby also extend the period for collection from appellant as a transferee?

The case presents no issue concerning an extension of the time for assessment of tax, since appellant has never claimed that the assessment was barred. However, since appellee appears to confuse the issue, citing cases which involve only the period for assessment in support of the District Court's decision in this case, it may be helpful to make quite clear the distinction between the two periods.

Under Section 275(a) of the Internal Revenue Code of 1939, income taxes must ordinarily be assessed within three years after the return was filed. This section provides:

“General Rule.—The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.”

Under Section 276(c), which is set forth at page 5 of appellant's opening brief, a Court proceeding to collect taxes is ordinarily barred unless commenced within six years after assessment. This is a separate period of limitation, which commences to run when the assessment is made.

Either of these periods may be extended by an appropriate agreement in writing between the Commissioner and the taxpayer, executed prior to the expiration of the period in question. Such agreements are commonly referred to as waivers. Waivers extending

the period for *assessment* are authorized under Section 276(b), while waivers extending the period for *collection* are authorized by Section 276(c).

Under Section 311(b)(1) of the 1939 Code, which is set forth at page 13 of appellant's opening brief, the period of limitation for assessment of tax against an initial transferee is "one year after the expiration of the period of limitation for assessment against the taxpayer." Since this one-year period does not commence to run until the expiration of the period for assessment against the transferor taxpayer, it is necessarily extended by waivers executed by the taxpayer extending that period. Appellee cites numerous cases which so hold, and with these we have no quarrel.

However, the period of limitations for assessment of tax is not an issue in this case. No assessment was ever made against appellant; the only assessment of these taxes was against The Mission Company, on October 10, 1947, and no action was taken to establish appellant's liability as a transferee until this suit was commenced on December 15, 1954. (By that time, it may be assumed, any assessment against appellant was barred by Section 311(b), and the Government could proceed, if at all, only by a suit in equity.)

The period of limitation involved here is that which bars a Court proceeding to collect tax if it is begun more than six years after assessment of the tax (Section 276(c)). The question is whether a waiver by the primary taxpayer, extending that six-year period for collection, also extended the period for a Court proceeding against appellant as transferee.

II. THE ATTEMPTED ANALOGY BETWEEN EXTENSIONS OF THE PERIOD FOR ASSESSMENT AND EXTENSIONS OF THE PERIOD FOR COLLECTION AFTER ASSESSMENT IS NOT VALID.

To the best of appellant's knowledge, the only reported decision which is squarely on the issue presented here is *United States v. City of New York, et al.* (S.D. N.Y., 1955), 134 F. Supp. 374, which is discussed in appellant's opening brief at pages 10 to 15, inclusive. None of the cases cited by appellee at pages 17 to 21 of its brief involved the issue of this case. On the contrary, all of those cases involved extensions of the period of limitation for *assessment*, as distinguished from *collection after assessment*, and they are in point only if an argument by analogy is ~~not~~ valid. It is appellant's position that the attempted analogy is not valid.

Appellee apparently relies on the supposed analogy, but without answering appellant's arguments on this point or explaining why it considers the analogy sound.

The decision in *City of New York* was expressly based upon this supposed analogy. There the Court said:

"There are analogous situations under the Code where voluntary unilateral action by the taxpayer-transferor tolls the statutory period as against his transferee. For example, an appeal to the Tax Court by the taxpayer suspends the limitation period—it also suspends the period for suits against his transferee. *Likewise a waiver agreement executed by the transferor extending the limitation period for assessments is valid as*

against his transferees.” (Italics added.) 134 F. Supp. at page 378.

The obvious difference is that the period of limitation for assessment against a transferee is, by statute, directly related to the period for assessment against his transferor, while the period for collection proceedings against a transferee is not similarly related to the period for collection proceedings against his transferor. Under Section 311(b)(1) of the 1939 Code the period for assessment against a transferee does not commence to run until “the expiration of the period of limitation for assessment against the taxpayer.” The Courts have properly held that any action by the primary taxpayer which extends the period for assessment against him delays the commencement of the period for assessment against his transferee, and thus extends that period.

There is no parallel relationship between the period of limitation for collection proceedings against the taxpayer and the period for such proceedings against his transferee. Section 276(c), which establishes the period of limitation for collection proceedings, makes no reference to transferees, providing generally that income tax may be collected by a proceeding in Court only if such proceeding is begun within six years after the assessment of the tax, or prior to the expiration of any extension of that period agreed upon in writing by the Commissioner and “the taxpayer”.

The *Updike* and *Markowitz* cases, cited at page 6 of appellant’s opening brief, make it clear that a suit against a transferee is subject to this six-year period

of limitation, and that the term "the taxpayer" in Section 276(c) must be understood to refer to the transferee, as well as to the transferor taxpayer. *Markowitz* held that a waiver signed by the transferee satisfied the requirement of an agreement by "the taxpayer", and extended the period for suit under 276(c).

Other reasons for concluding that the attempted analogy is invalid are argued at pages 14 and 15 of appellant's opening brief, and need not be repeated here.

III. THERE IS NO EVIDENCE IN THIS CASE OF ANY ADMINISTRATIVE PRACTICE REGARDING EXTENSIONS OF THE PERIOD FOR COLLECTION OF TAX.

Appellee urges that its position in this case is supported by an established administrative practice (Br. 17). But there is no evidence in this case of any such practice, nor do the cases cited by appellee in support of this proposition indicate any such practice. All of those cases relate exclusively to the period of limitation for *assessment*, as distinguished from the period for *collection after assessment*.

In answer to appellant's argument distinguishing between extensions of the two statutory periods, appellee calls particular attention to *Rite-Way Products, Inc. v. Commissioner* (1949), 12 T.C. 475 (Br. 18). However, that case, like the others cited by appellee, involved waivers extending the period for assessment. The reference in the quoted portion of the Tax Court's opinion (Br. 18) to consents extending "the period

of limitations for assessment and collection" clearly has to do with waivers authorized under Section 276(b), and not with waivers extending the period for collection after assessment, authorized under Section 276(c), which are at issue in this case.

The case of *United States v. Markowitz* (N.D. Cal., 1940), 34 F. Supp. 827, which is cited and discussed in both appellant's opening brief (pp. 6, 12) and appellee's brief (p. 23), may well indicate an administrative practice of extending the period for collection after assessment by obtaining waivers from transferees, and not relying upon waivers executed by transferor taxpayers.

IV. STATUTES OF LIMITATION BARRING THE COLLECTION OF TAXES SHOULD BE LIBERALLY CONSTRUED IN FAVOR OF THE TAXPAYER.

In our opening brief we argued (pp. 11-12) that statutes of limitation barring the collection of taxes are to be construed liberally in favor of the taxpayer, and that Judge Weinfeld was mistaken in stating a contrary rule of law in *City of New York*. Appellee takes issue with this (Br. 16), and maintains that the rule was correctly stated in *City of New York*.

In support of our position we cited three cases:

Bowers v. New York & Albany Company
(1927), 273 U.S. 346, 47 S.Ct. 389;

United States v. Updike (1930), 281 U.S. 489,
50 S.Ct. 367;

Commissioner v. Bryson (C.A. 9, 1935), 79 F.
2d 397.

In each of these cases the Court acknowledged the rule that provisions of limitations embodied in taxing acts are to be construed liberally in favor of the taxpayer.

In contending to the contrary, appellee cites four cases and quotes from Mertens, Law of Federal Income Taxation (Br. 16, 17). Appellee relies upon the following cases:

DuPont de Nemours & Co. v. Davis (1924), 264 U.S. 456, 44 S.Ct. 364;

Pacific Coast Steel Co. v. McLaughlin (C.A. 9, 1932), 61 F. 2d 73, affirmed 288 U.S. 426;

McCarthy Co. v. Commissioner (C.A. 9, 1935), 80 F. 2d 618, cert. den. (1936), 298 U.S. 655;

and

Loewer Realty Co. v. Anderson (C.A. 2, 1929), 31 F. 2d 268, cert. den. 280 U.S. 558, 50 S.Ct. 17.

The *DuPont* case is immediately distinguishable, since it did not involve a tax statute. In that case the Government's Director-General of Railroads sued to recover demurrage charges on certain shipments of cotton linters, and the issue was whether the action was barred by a three-year statute of limitations applicable to actions by carriers. The Supreme Court held that the statute did not apply to actions brought by the Government.

Pacific Coast Steel Co. v. McLaughlin, a Ninth Circuit case, was decided three years before *Commissioner v. Bryson*, upon which we rely, and must be considered overruled by *Bryson* on the point under discussion.

It is true that in the *McCarthy* case this Court quoted from Mr. Justice Sutherland's opinion in *DuPont* the statement, "Statutes of limitation sought to be applied to bar rights of the Government, must receive a strict construction in favor of the Government." (80 F. 2d at 620). However, *McCarthy* was decided by this Court less than four months after its decision in *Bryson*, and the Court's opinion in each case was written by Judge Garrecht. The opinion in *McCarthy* contains no reference to *Bryson*, and it should not be easily assumed that the Court intended to reverse the rule approved in *Bryson*, in view of these facts. As has been shown, the *DuPont* case, from which the quotation is taken, did not involve a tax statute. *McCarthy* itself involved the effect of a waiver extending the period for assessment which the parties had stipulated was "executed" by the taxpayer, but which the taxpayer claimed had not been properly filed or consented to by the Commissioner.

Loewer Realty Co. was decided in the Second Circuit in 1929, prior to the Supreme Court's decision in *Updike* and the *Bryson* case in this Court, upon which we rely.

There must still be considered the passage quoted from Mertens in appellee's brief (p. 17, footnote 2). This is apparently appellee's sole authority for the statement that "since deciding the *Bowers* case, the Supreme Court has been active in stopping attacks based on the statute of limitations which have been made following its ambiguous statement in that case." (Br. 16). Appellee cites not one Supreme Court deci-

sion in support of this statement, and the only Supreme Court case cited by Mertens as evidence of any change of position since the *Bowers* case is *Stearns v. United States* (1934), 291 U.S. 54, 54 S.Ct. 325.

The *Stearns* case was a taxpayer's suit for refund. The issue presented was whether an assessment was invalid where the waiver relied upon by the Government had been signed by the taxpayer, but not by the Commissioner. It was held that the evidence supported a finding that the Commissioner had approved the extension in writing, as required by the Code, and that, in any event, the taxpayer was estopped to assert the statute of limitations. The opinion does not discuss the question of whether the statute of limitations is to be strictly construed in favor of the government or the taxpayer, nor does it cite *Bowers* or *Updike*.

It is submitted that the Supreme Court's statement in the *Updike* case, approving "the rule which requires taxing acts, including provisions of limitation embodied therein, to be construed liberally in favor of the Taxpayer," remains a correct statement of the law on this point. This view was accepted by this Court in *Bryson* in 1935, and neither the Supreme Court nor this Court has seen fit to change its view. Merten's statements to the contrary must be regarded as editorial comment rather than a statement of the law.

CONCLUSION.

The issue presented in this appeal has been considered in only one reported decision: *United States v. City of New York*, decided in the District Court for the Southern District of New York in 1955. That case was incorrectly decided, and should not be followed.

This suit against appellant was barred by the six-year statute of limitations, under Section 276(c) of the Internal Revenue Code of 1939, and the judgment should therefore be reversed and judgment entered in favor of appellant.

Dated, Oakland, California,
November 18, 1957.

Respectfully submitted,

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By J. RICHARD JOHNSTON,

Attorneys for Appellant.

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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MINEZ NORTES, VICTOR RODRIGUEZ,
MANUEL FERNANDEZ RODRIGUEZ and
UGUSTIN CABRERA OROZA,

Appellants,

vs.

HARLES C. HARTMAN, and
ALBERT DEL GUERCIO,

Appellees.

APPEAL FROM
UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF CALIFORNIA, CENTRAL DIVISION
HON. THURMOND CLARKE, PRESIDING

APPELLANTS' REPLY BRIEF

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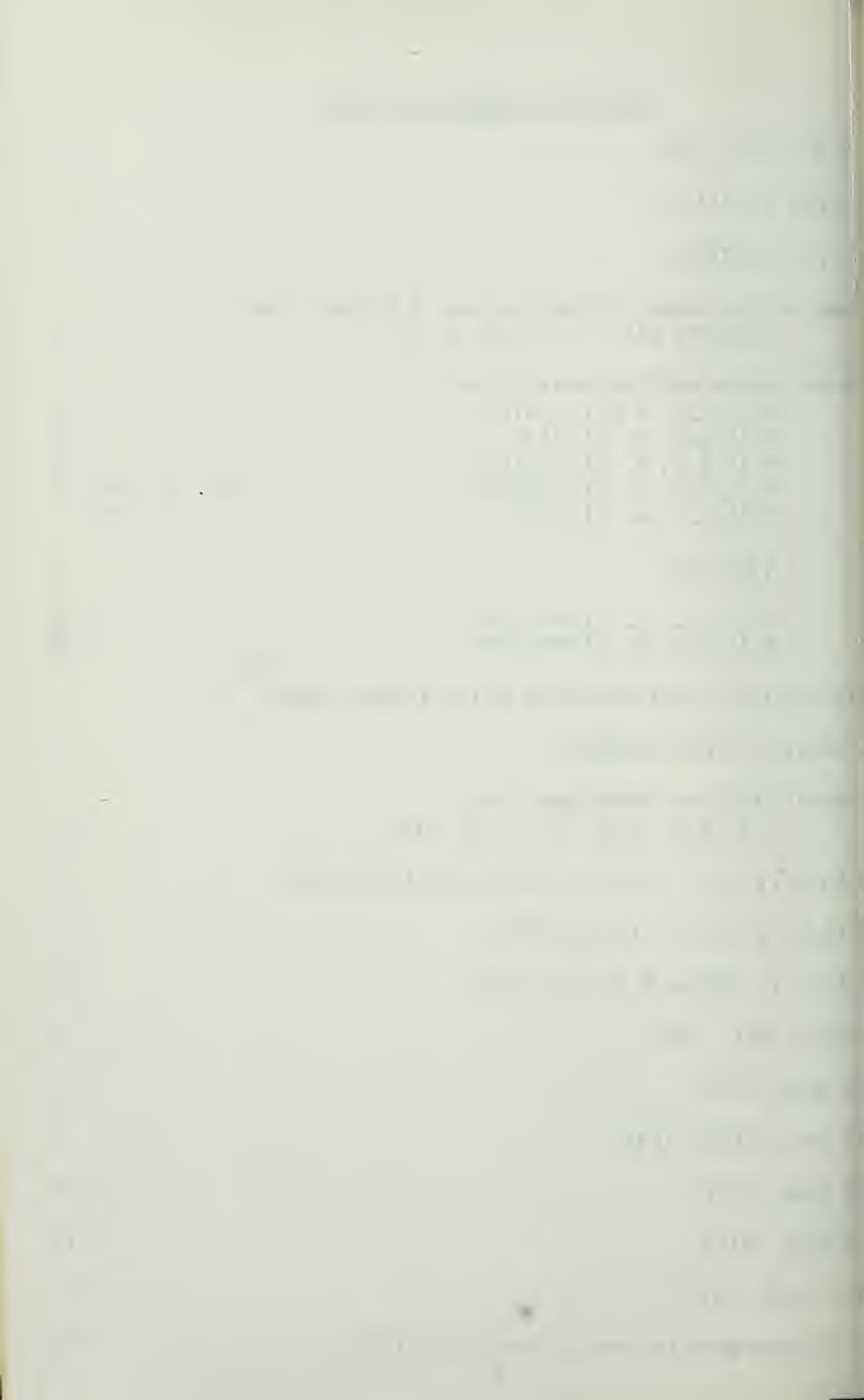
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APPELLANTS' REPLY BRIEF

I.

THE MANIFEST INTENTION OF THE PARTIES
TO THE 1902 TREATY WAS TO CONFINE
APPLICATION OF ARTICLE XXIV THEREOF
TO DESERTIONS OCCURRING WITHIN THE
ASYLUM COUNTRY.

A.

The Language of Article XXIV is Unambiguous,
and Fully Defines The Reach Which The
Parties Thereto Intended to Give It.

Without quite saying so, Respondents 1/ strain for a

1/

The use of the term "respondents" herein instead of
appellees is to avoid confusion with the term "appellants".



broader than that clearly indicated, manifestly its scope must stop at our borders. Under no construction that is fair and reasonable could Article XXIV be stretched to embrace seamen deserting beyond the territorial limits of the United States (United States v. Curtis-Wright, 299 U. S. 304; The Apollon, 22 U. S. 159).

Moreover, under this treaty, seamen may be arrested without a warrant, and detained without a hearing. Even aliens are entitled to due process of law (Kwong Hai Chew v. Colding, 340 U. S. 590), and it cannot be assumed, in the absence of a more precise mandate, that the United States obligated itself to the application of such harsh and offensive measures beyond the limits of practical necessity (52 Am. Jur., §34, p. 826).

The government argues, however, that under appellants' theory, "... it would only be necessary for a crewman while on shore leave to pass beyond the geographical limits of the port' to immunize himself from arrest." (Emphasis supplied). Respondents overstate the alternative. Alien seamen are always amenable to arrest by the Immigration Service for violation of the United States immigration laws (See: Immigration and Nationality Act, §§251-257; 8 U. S. C. A. §§ 1281-287). But we are dealing here with the applicability of a treaty provision, the arrest and detention provisions of which depart markedly from our traditional concepts of due process

and equal protection of the laws. Thus, the draftsmen of the 1902 treaty assigned the task of administering Article XXIV only to those officials located within the city limits of the port; and enforcement of this provision need not - and does not - befall the duty of officials throughout the United States unless the parties to the treaty say so much more explicitly than they have here.

Finally, respondents argue that appellants deserted in San Diego in any event because they acquired permission to leave the ship by fraud which vitiated their leave status at its inception (Resp. Br. p. 9). This contention would be better served had appellants been charged with criminal conspiracy which makes punishable an unlawful agreement whether or not the contemplated crime is consummated (United States v. Boyer, 331 U. S. 532, 542). However, the allegedly fraudulent procurement of their leave would go only to the question of intent, whereas the offense of desertion, as we pointed out in our opening brief (pp. 20-24), requires, additionally, the overt act of absence without leave. Appellants may very well have changed their minds several times before actually overstaying their leaves with an intention not to return (See: R. 40, 57.) Indeed, appellant RODRIGUEZ did just that in Panama (R. 39.) Thus, the offense of desertion could not be complete until appellants' leave had expired which, in this case, did not occur until they reached a point far beyond the city limits



of San Diego.

The cases relied upon by respondents as supporting their fraud theory (Resp. Br. p. 9) ^{4/} are distinguishable for the reason that the courts there were reaching "stealthy encroachments against the constitutional rights of citizens" by public officials, in order to effectuate public policy against unreasonable searches and seizures (Fraternal Order of Eagles No. 778 v. United States, 57 Fed.2d 93, 94). Nor is respondents' reference to the Manual for Courts-Martial of the United States relevant here, because that treatise is concerned only with desertions from the United States military forces; and furthermore, because it cannot be said that appellants committed an act inconsistent with their leave status until they crossed the border into Mexico - at which point the Treaty of 1902 became inapplicable.

4/ Gouled v. United States, 255 U. S. 298;

Fraternal Order of Eagles, No. 778 v. United States, 57 Fed.2d 93.

The Construction of Article XXIV Urged By
Appellants Does Not Jeopardize the 1902
Treaty, or Any Other.

In its preliminary statement, the Government pleads for a ruling upholding the 1902 Treaty in that the United States has similar treaties with Greece and Columbia. (Resp. Br. p. 7). An adverse ruling, so the argument runs, "might cause other nations to become apprehensive that our judiciary will not honor similar agreements with them; and that they might be 'entirely stripped of their crews in '" United States ports (Tucker v. Alexandroff, 183 U. S. 424, 430) (Resp. Br. p. 8).

Any such apprehension would be entirely unfounded. Examination of our commercial treaties with Greece and Colombia, as well as that with Russia involved in Tucker v. Alexandroff, supra, all contain language providing for the arrest and detention of deserting seamen of the respective countries wherever in the United States they may be found. ^{5/}

^{5 /} Thus: Article XIII of the Convention between Greece and the United States of 1902 (proclaimed in 1903), (33 Stat. 2122, 2131), authorizes the "arrest, detention and imprisonment of the deserters from the ships at war and merchant vessels of their country ..."

The treaty with Russia, found in Tucker v. Alexandroff, supra, at p. 429, contained the identical provision.

And Article XXXIII of the Treaty with New Granada (Colombia) of 1846, 9 Stat. 881, 896, permits "the arrest, detention and custody of deserters from the public and private vessels of their country ..."



II

THE EXTRADITION TREATY, AND PARTICULARLY ARTICLE III THEREOF, IS APPLICABLE TO THE CASE AT BAR.

A.

Article III is Not Limited To Crimes Enumerated in the 1904 Treaty, But By Its Express Terms, Applies to Any Demand Made By Spain For Return of Its Citizens.

Respondents contend that the Extradition Treaty of 1904 is, by definition, inapplicable to the case at bar, thereby rendering it unnecessary to consider appellants' claims that their "desertion" was of a political character (Resp. Br. pp. 14-15). This argument hangs by the notion that the appearance of Article III in a treaty denominated by, and using the term "Extradition" confines its application to those crimes enumerated in that convention which were committed upon territory of the demanding state. 6/

The Government's reliance upon Terlinder v. Ames (184 U. S. 270, 276) to support its thesis is misplaced. Both the treaty and the statute involved in Terlinder expressly

6 / Under this definition, of course, respondents' theory that appellants' desertion commenced on board their ship by virtue of their concealment of their plans (Resp. Br. 9), places appellants' desertion on Spanish territory and thus, within the Extradition Treaty as well (I Moore, on Extradition, p. 136).

preclude the forcible repatriation of persons accused of political crimes; it also constitutes an acknowledgment that such policy pre-dated the treaty. This is understandable, for when the Extradition Treaty was finally proclaimed (in 1908), the Statue of Liberty - itself a recognition of our historical traditions - had already been welcoming the oppressed of other lands for twenty-four years. Thus, to narrow the scope of Article III so as to exclude "deserting" seamen whose only crime is their love of liberty, is to drain that provision of its history and purpose. To paraphrase Chief Justice Goddard in Ex Parte Kolczywski: ^{7/}

"The evidence about the law prevalent in [Franco Spain] today shows that it is necessary, if only for reasons of humanity, to give a wider and more generous meaning to the words we are now construing, which we can do without in any way encouraging the idea that ordinary [desertions] which have no political significance will be thereby excused."

In the absence of far more convincing treaty language than that which appears at bar, it is inconceivable that the

^{7 /} Case of the seven Polish seamen: 1954, 2 Weekly Law Reports, 116 (1955); 1 ALL. E. R. 31; cited in Karadzole v. Artukovic (CCA 9) 247 Fed. 2d 198, at p. 203).

mere procedure for restoring a fugitive to the jurisdiction of the demanding state, rather than the character of his crime, was intended to control the applicability of Article III (See: Valentine v. United States, supra). We submit, therefore, that Article III of the 1904 Extradition Treaty is applicable to the case at bar.

B.

Treaties, Like Statutes, Are Subject To
Judicial Construction, And To Hold That
Article III Bars Spain's Right to Reclaim
Appellants In No Sense Constitutes A
Political Decision

At the outset, it must be noted that respondents do not deny that Spain is controlled and dominated by a ruthless dictator, who for twenty years has crushed all religious and political dissent by force and violence; or that appellants abandoned their ships in order to escape from Franco Spain, and seek freedom elsewhere; or that their forcible repatriation to Spain would subject them to physical persecution and possible death because of what they have said and done about Franco. 8/

3/ See App. Br. pp. 32-33, and Appendix A and B.
NOTE: Appellants gratefully acknowledge their indebtedness to Drs. Victoria Kent (of New York), Dwight L. Bolinger, Jacques C. Antoine, and Laudelino Moreno (of Los Angeles), for furnishing material and facts about conditions in Franco Spain.

The Government's only reply to all this is that the recognition of Spain by the United States bars judicial inquiry into the character of that regime (Resp. Br. pp. 16-17). This argument is a non sequitur. Although the Court undoubtedly has the power to compel the Attorney General to exercise his discretion where he is under a duty to do so, 9/ that is not the issue here. Nor is this Court being asked to interfere with a political decision of the executive or legislative branches of government. 10/

The question at bar is whether Spain has a legal right to demand appellants' repatriation, and the correlative duty of the United States to comply therewith. Accordingly, "to determine the nature and extent of the right," this Court must look at the treaties which create or delimit it (Factor v. Laubenheimer, 290 U. S. 276, 287.) Thus, recognition of Yugoslavia by the United States, and the existence of several

1/ See Savala-Cisneros v. Landon, 111 Fed. Supp. 129, 131; cf. Williams v. Fanning, 332 U. S. 490.

0/ Because no such decision has been made. However, there is a question as to whether a decision to remand appellants to Franco Spain would not constitute a deprivation of appellants' right to life and liberty without due process of law under the Fifth Amendment to the United States Constitution, particularly in view of our public policy against the forcible return of political refugees to totalitarian regimes where there is a likelihood they will suffer political persecution there (See: App. Br. pp. 29-35.) (cf. Valentine v. United States, 299 U. S. 5, 9).

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mutual defense pacts between the two nations, 11/ did not preclude this Court from holding that under an extradition treaty, a Yugoslav citizen was not extradictable as a war criminal because his crimes were of a political character (Ivancevic v. Artukovic, 211 Fed. 2d 565; cert. denied), 348 U. S. 818; Karadzole v. Artukovic, 247 Fed. 2d 198).

The point is, that the United States has not refused to grant appellants political asylum. Rather it has studiously avoided reaching that question by insisting that the government is bound by the 1902 Treaty to deliver appellants to Spain because Article III of the Extradition Treaty is inapplicable. It is reasonable to infer that the same rationale served as the basis for the District Court's order. In view of the political

11/ See: Agreement governing the furnishing of assistance under the Yugoslav Emergency Relief Assistance Act of 1950, signed at Belgrade January 6, 1951 (2 U. S. T. 13; T. I. A. S. 2174; 122 U. N. T. S. 137); Agreement relating to supplies of food for Yugoslav armed forces, furnished under the Mutual Defense Assistance Act, entered into force November 21, 1950 (I. U. S. T. 753; T. I. A. S. 2145); Agreement relating to the furnishing by the United States to Yugoslavia of raw materials and other supplies to support the material requirements of the Yugoslav armed forces - entered into force April 17, 1951 (2 U. S. T. 2254; T. I. A. S. 2349); Agreement regarding military assistance, signed at Belgrade, and entering into force on November 14, 1951 (2 U. S. T. 914; T. I. A. S. 2245); Agreement relating to the disposition of redistributable and excess military assistance property in Yugoslavia, entered into force May 22, 1955; Agreement relating to special program of facilities assistance pursuant to the military assistance agreement, entered into force September 30, 1955 (T. I. A. S. 3370).

character of appellants' offense, however, it is plain that Article III of the 1904 Treaty denies Spain a right to claim appellants, and in the event a claim is made, relieves the United States of any duty to honor it. 12/

III.

RESPONDENTS ARE WITHOUT JURISDICTION TO DETAIN APPELLANTS OR TO DELIVER THEM TO THEIR SHIPS.

As suggested in Appellants' Opening Brief (beginning p. 36), there are at least four reasons why respondents have never acquired, and do not now have, jurisdiction to detain appellants or to deliver them to their ships pursuant to the 1902 Treaty. First, respondents lacked the requisite statutory authority for paroling appellants into the United States; Second, by virtue of their parole, appellants are still in

12/ Although not heretofore referred to, judicial cognizance should also be taken of the Constitution of the International Refugee Organization, to which the United States is a signatory party (62 Stat. 3037), which defines as political refugees inter alia:

(b) Spanish Republicans and other victims of the falangist regime in Spain, whether enjoying international status as refugees or not:

(Annex I, Part I, Section A-1 (b), - 62 Stat. 3049)

By this agreement, the United States has pledged its assistance in relocating political refugees from Spain "until the time when a democratic regime in Spain is established" (62 Stat. 3038).

Mexico in contemplation of law, and so respondents do not have jurisdiction over their persons such as to enable them to give effect to the 1902 Treaty; Third, appellants voluntarily entered the United States as a result of fraud, deception and unlawful exercise of authority by respondents' subordinates; and Fourth, the government was without power to seize and detain appellants.

We now proceed to meet the government's counter-arguments on these points:

A.

Appellants Were Unlawfully Paroled Into
The United States.

1.

Respondents Attempted to Parole Appellants
Into The United States, and Whether or Not
Appellants Were Deported From Mexico is
Irrelevant.

Respondents advance the amazing theory that appellants were not paroled into the United States "since on July 5, 1957 appellants were deported from Mexico," and "having thus been deported, appellants were lawfully in the custody of the United States Immigration and Naturalization Service . . ." (Resp. Br. p. 18).

We fail to see how appellants' alleged deportation by Mexico conferred jurisdiction upon respondents. It had been

our assumption that only laws of the United States could do that (Valentine v. United States, supra, p. 9; Semble; Federal Trade Commission v. Raladam Co., 283 U.S. 643). And United States statutes are quite clear on the subject: Any alien not in possession of a valid immigration visa or entry permit "shall be excluded from admission into the United States" (Emphasis supplied) (8 U. S. C. A. §§ 1181 (a), 1182 (a) (20); 8 C. F. R. 211.1, et seq. and 235.1 et seq). Obviously, United States Immigration officials could not admit appellants into the United States, unless empowered by law to do so. Whatever may have been respondents' manifest intentions (Resp. Br. p. 19) §212 (d) (5) of the Immigration and Nationality Act (8 U. S. C. A. 1182 (d) (5)) is the only law to our knowledge which permits the entry of aliens without valid immigration documents - and then, only under special emergent circumstances. Irrespective of whether or not the Immigration Service contemplated an application of §212 (d) (5), that was the document which they in fact selected, and the only law under which they had authority to act. Respondents' claims that they could have invoked other authority to effect appellants' entry into the United States may therefore be disregarded, since they point to none (Resp. Br. 18-19).

There Is No Competent Evidence In The
Record At Bar Of Appellants' Deportation
from Mexico.

Nevertheless, respondents deposit so much of their reasoning upon the alleged deportation of appellants by Mexico, that we pause briefly to expose the error of this claim.

The only evidence of alleged deportation is Exhibit "G", consisting simply of a letter written in Spanish by an official of the Mexican Immigration Service to a United States Immigration officer, purporting to state that appellants were deported from Mexico pursuant to an Order of the Secretary of Interior of Mexico. This exhibit was received into evidence, untranslated, ^{13/} over the vigorous objections of appellants (R. 87-88). The utter incompetency of that document as evidence of a deportation is manifest:

First, it is replete with bare legal conclusions, is not the best evidence, and is not even an official certificate such as might come in under an exception to the hearsay rule.

"The general governing rule is that official certification of a fact drawn or gathered from a public record is a mere legal conclusion, or

^{13/} Counsel for appellants did not see this document until shortly before it was introduced into evidence; and did not obtain an accurate translation thereof until after the trial (See: R. 86).

the opinion of the certifying officer, and so not admissible as evidence. He should copy the record verbatim, certifying that he has done so, and that the copy is an accurate transcript of the original." (U. S. Slicing Mach. Co. v. Wolf, Sayer & Heller, Inc., (D. C. Ill., 1917), 243 Fed. 412, 413; aff'm'd 257 Fed. 93). ^{14/}

Secondly, no foundation was laid for the receipt of the exhibit into evidence since the document was not translated, and its admission in that form deprived appellants of their right of confrontation (V Wigmore On Evidence (3rd Ed), §1393, p. 117).

And thirdly, no foundation was laid, and it does not appear therefrom, as to whether the officer who signed the letter was the custodian of the records from which the alleged facts were drawn (See: Esnault-Pelterie v. Chance Vought

^{14/} Accord: United States v. Grabina (CCA 2d, 1941), 119 Fed. 2d 863, 865 (certification by Mayor of Polish town declaring records revealed party was married there, held inadmissible); In Re Asterios Estate (1939), 16 N. Y. S. 2d 943, 945, 172 Misc. 1081 (Certificate by Mayor of Greek town as to persons and births appearing in Municipal Registry, held inadmissible); Pekin Cooperage Co. v. State (Sup. Ct. Ark.), 197 Ark. 341, 122 S.W. 2d 468, 470 (Certificate by Secretary of State that corporation did not exist, held inadmissible).

Corp. (D. C. N. Y. 1932) 56 Fed. 2d 393, 396, aff'm'd 66 Fed. 2d 474).

Clearly, then, D'Agostino v. Sahli (230 Fed. 2d 668 (5th Cir. 1956)), must be distinguished from the case at bar, since there is no competent evidence before this Court that appellants were deported from Mexico, or that the Mexican Government officially cooperated in their surrender to American authorities. Indeed, the official position of Mexico belies any such inference.

B.

The 1902 Treaty Is Inapplicable Because
Appellants Are Legally Still in Mexico
And Therefore Beyond Its Reach.

From the foregoing discussion, it is apparent that appellants were paroled into the United States (albeit unlawfully), in legal consequence of which they are still in Mexico. Accordingly, they are beyond the reach of the 1902 Treaty, and cannot be delivered to their ships. (See App. Br. pp. 36-44).

Respondents seek to avoid this result by arguing that appellants were "never legally admitted to Mexico," and that "mere temporary presence in that country would not be effectual to place their juridical persons there." (Resp. Br. p. 20).

Although there is no competent evidence in the record at bar bearing on whether or not appellants were "legally admitted to Mexico," neither their alleged illegal entry therein or the duration of their stay there defeats their status as subjects of Mexico. Appellants entered Mexico for the avowed purpose of establishing a domicile, and with the intention to remain there (See: e. g., R. 53, 55, 62). Absent evidence to the contrary, it was unnecessary for appellants to obtain authorization from Mexico in order to acquire a new domicile in that country (Harral v. Harral, 39 N. J. Eq. 279). Furthermore, their length of residence, no matter how brief, is irrelevant once domicile has been established (Schillerstrom v. Schillerstrom, 75 N. D. 667, 32 N. W. 2d 106; 17 Am. Jur. §20, p. 603). Having thus successfully acquired domicile in Mexico, appellants - even though strangers - placed themselves under the protection of Mexican sovereignty (See: Fong Yue Ting v. United States, 149 U. S. 698, 724). Since under United States law, and by the term and conditions of their parole (See: Exhibit 1), appellants have never legally entered the United States, it follows they are yet in Mexico, under the protection of the sovereignty of that country. (Compare: Fong Yue Ting v. United States, supra, p. 724). Respondents therefore can apply the 1902 Treaty to appellants - i. e., seize and detain them - only by "kidnapping" them from Mexican territory. Since the United States has an extradition treaty

with Mexico (31 Stat. 1818), appellants' recovery must be sought by adhering to the procedures provided in such treaty (Cook v. United States, 288 U. S. 102, 120-122; United States v. Ferris, 19 Fed. 2d 925; Collier v. Vaccaro, 51 Fed. 2d 17).

In the meanwhile, the 1902 Treaty being inapplicable, appellants must be restored to Mexican territory by virtue of the "parole" statute (8 U. S. C. A. §1182(d) (5); See also: United States v. Rauscher, 119 U. S. 407). Respondents are without authority to dispose of them in any other way.

The fact that the 1902 Treaty does not require a crew-man to be "within the United States" is beside the point (Resp. Br. p. 21). As we said in our opening brief, that treaty can be operative only within the territory of the signatory countries, and only upon the persons found therein (App. Br. pp. 41-42). Whether a deserter would ordinarily be "within the United States" in legal contemplation is not before this Court, although the means of dealing with such persons is amply provided for by our statutes. 15/

15/ See: §§251-257, Immigration and Nationality Act, (8 U. S. C. A. §§1281-1287).

C.

Respondents Did Not Acquire Jurisdiction
Over Appellants In That The Latter
Entered The United States Only Because
of The Deception, Fraud and the Unlawful
Exercise of Authority by Respondents'
Subordinates and Agents.

Jurisdiction over an alien is had by the Immigration Service when he is found in territory of the United States. But it cannot be said that he is so found there when the alien is enticed into American territory by fraud, trickery or illicit practices of the Immigration Service, or persons acting in its behalf (cf. Blandin v. Ostrander, (CCA 2, 1917), 239 Fed. 700). Jurisdiction cannot be invoked by ruse or by misuse of a statutory authority, since it would then rest upon fraud or some other illegal act (Blandin v. Ostrander, supra).

Appellants had not violated any law of the United States, nor were they accused of such offense (compare: D'Agostino v. Sahli, 5th Cir., 1956), 230 Fed. 2d 668). Yet, an officer of the United States Navy accompanied the Spanish captain of the "El Mirante Ferrandiz" across the border to enable the latter to persuade appellants to return to their ships (R. 91, 92). Why the United States Navy found it necessary to lend its prestige to the Spanish captain is not fully explained by the record. 16/

16/ The government simply says that the officer went as a "guide". See: Answer, Para II (y), at p. 2, line 17).
22.

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When, however, that effort proved unsuccessful, officers of the United States Immigration Service whisked appellants from Mexican territory by means of an Order of Parole (Exhibit 1). This was accomplished before either respondents or their subordinates had received a written demand from the Spanish Consul, and prior to their receipt of a manifest from the captain of the deserted ships (App. Br. p. 14, fn. 21).

Moreover, while such Order of Parole required an application by appellants for permission to enter the United States, respondents concede that none was obtained (Resp. Br. p. 19; See also, R. 24-25).

Although respondents now deny that they intended Exhibit I to serve as an Order of Parole (Resp. Br. p. 19), their subordinates apparently felt the necessity of securing the signature of appellant ENRIQUE FERNANDEZ thereto. The uncontroverted evidence shows how this was accomplished:¹⁷

"Q by Mr. Wirin: Now, I show you Petitioners' Exhibit No. 1 and call your attention to a writing which reads "Enrique Medina" on the reverse side and ask you if that is your handwriting?

A. Yes. It is my handwriting.

Q. Where was the document signed?

17/ At R. 58-59.

A. In the American Immigration.

Q. How many American Immigration officers were there, at the time you signed this paper?

A. One only. There was a man there.

Q. Did he read this paper to you before you signed it?

A. No.

Q. Did you know what you were signing?

A. BY THE WITNESS: No.

THE INTERPRETER: "No."

Q. By Mr. Wirin: Can you read English?

A. THE WITNESS: No.

THE INTERPRETER: "NO."

Q. By Mr. Wirin: What did you understand that you were signing?

A. Well, I don't know; I did not know anything about it. I thought something about the ship, where they were going to send me. I did not understand it; I did not understand it at all.

Q. Did you, at any time, when you were in custody of United States Immigration, on July 5, 1957, desire to come into the United States from Mexico?

A. No, I wanted to go to Mexico."

All the surrounding circumstances considered, it is



submitted that the entry of appellants into the United States did not confer jurisdiction upon the respondents to seize or detain them under the 1902 Treaty.

D.

Respondents Were Without Power To Seize
Appellants, And Therefore Are Without
Power to Detain Them, or Deliver Them
To Their Ships.

There is, however, a more fundamental jurisdictional defect which the government has chosen to ignore. Respondents relied upon the 1902 Treaty as authority for their seizure and detention of appellants as deserters. As previously stated, however, a treaty is applicable and enforceable only within the territorial limits of the signatory nations (United States v. Curtis-Wright, 299 U.S. 304; The Apollon, 22 U.S. 159 (9 Wheat 362)). As a matter of fact, it is clear from the language of Article XXIV of the 1902 Treaty that no more was intended by either party thereto. This being so, Article XXIV confers jurisdiction upon competent officials of the asylum state to arrest and detain only those deserters actually found in their country.

Yet, it is evident from previous discussion that appellants were found in Mexico - not only in the sense of discovery, but within the meaning of seizure. That is to say, appellants were paroled by respondents into the United States against their will,

in violation of American law, and without consent of the Mexican government. Moreover, Spanish authorities had themselves failed, at that point, to comply with the provisions of Article XXIV requiring the submission in writing of a demand, accompanied by the ship's manifest, to the arresting officers. In short, though purporting to act under the 1902 Treaty, respondents failed to conform to its provisions and limitations.

Here, then, we have a case falling squarely within the principle of Cook v. United States, 288 U. S. 102. There, the Coast Guard seized the *Mazel Tov*, a British vessel carrying contraband while hovering eleven and a half miles off our coast. Such seizure was authorized under then existing United States law empowering the Coast Guard to board any vessel suspected of carrying illicit merchandise, within four leagues (twelve miles) of the coast, and if upon search and examination of the cargo it appeared that any United States law was violated, the vessel or merchandise was liable to forfeiture. A treaty between the United States and Britain, however, authorized such boarding and search of British vessels only one hour's distance from shore. Since the *Mazel Tov* was capable of speeds of only ten miles per hour, the seizure was held unlawful. In so holding, Justice Brandeis declared for the majority:

"The objection to the seizure is not that it was

wrongful merely because made by one upon whom the government had not conferred authority to seize at the place where the seizure was made. The objection is that the Government itself lacked power to seize, since by the treaty it had imposed a territorial limitation upon its own authority. "
(P. 121).

The theory behind Cook seems to be that the United States had limited its sovereignty, respecting the ship *Mazel Tov*, to a point ten miles from shore. Obviously, the Coast Guard could not claim a power which the United States government had itself forsaken.

So here, the United States has delimited its sovereignty in two respects: First, by the terms of Article XXIV of the 1902 Treaty; and Second, by its Extradition Treaty with Mexico. 18/ Both of these treaties provided for the exclusive remedy for the recapture of fugitives. It is true that the failure to comply with the 1902 Treaty did not offend Spanish sovereignty. But it is no less true that the failure of the United States to resort to its Extradition Treaty with Mexico in seeking to capture a fugitive residing there offended Mexican sovereignty (Valentine v. United States, supra; United States

18/ - Extradition Treaty of 1899 between Mexico and the United States, 31 Stat. 1818.

v. Rauscher, 119 U. S. 407, 419-421; Collier v. Vaccaro, 51 Fed. 2d 17.) Therefore, once appellants had reached Mexico, respondents' only recourse was to obtain their return by making proper demand upon Mexico under the Extradition Treaty of 1899. Since, however, respondents, and their subordinates, took matters into their own hands, without resort to the diplomatic procedures provided in the treaty with Mexico, they thereby exceeded the limits of national sovereignty which the United States had imposed on itself. It follows that respondents were without power to seize appellants from Mexican territory. And absent a power to seize, jurisdiction could not be conferred upon the arresting officers simply because they now have custody of the appellants (Cook v. United States, supra, at p. 121).

Moreover, whereas in the Cook case, the Coast Guard was at least armed with statutory authority, here respondents had none. Without the power and authority of either law or treaty to seize appellants, they cannot have jurisdiction to detain them or deliver them to their ships.

IV

UNLESS APPELLANTS ARE RESTORED
TO MEXICAN TERRITORY, THEY ARE
ENTITLED TO THE RELIEF AUTHORIZED
BY SECTION 243 (h) OF THE IMMIGRA-
TION AND NATIONALITY ACT

Respondents assign two reasons for the purported inapplicability of §243(h) of the Immigration and Nationality Act (8 U. S. C. A. §1253 (h)). The first is that this section was never "intended to override the obligation imposed by Article XXIV" of the 1902 Treaty.

On the contrary, as we have attempted to show at great length, the provisions of Article III of the 1904 Extradition Treaty evidence expressly authorize asylum for citizens of the demanding nation who have committed crimes of a political character. Section 243 (h) simply implements Article III by affording the government a procedure for determining whether appellants are bona fide political refugees entitled to asylum in this country, if not in Mexico.

Next, respondents contend that appellants are not eligible for discretionary relief because they are not aliens "within the United States" within the meaning of §243(h), of the Immigration and Nationality Act. We submit that if the appellants are within the United States for the purposes of satisfying the 1902 Treaty, they are certainly here within the meaning of §243(h) (Quan v. Brownell, No. 12772 __ Fed. 2d __,

detain, examine and deport any aliens who enter the United States voluntarily or otherwise (Resp. Br. pp. 25-26).

It has been seen, however, that the 1902 Treaty is the authority under which the respondents purported to seize and detain appellants (See Exhibit I). If the 1902 Treaty is inapplicable, then each appellant having been paroled into the United States, must "forthwith . . . be returned to the custody from which he was paroled . . ." (§212(d) (5) Immigration and Nationality Act; 8 U. S. C. A §1282 (d) (5).)

D'Agostino v. Sahli (CCA 5, 1956), 230 Fed. 2d 668, upon which respondents rely so heavily, is not in point, first, because there is no competent evidence at bar that appellants were deported from Mexico; and secondly because appellants were paroled into the United States, and hence, did not "enter" within the meaning of the term "entry" as defined in 8 U. S. C. A. 10 (a) (13).).

B.

A Writ of Habeas Corpus Will Lie Not Only
To Test The Legality of Appellants'
Detention, But The Propriety of Their
Disposition.

Respondents err in stating that a Writ of Habeas Corpus does not lie in the event they have legal custody. The District Court's order directs the delivery of appellants to their ships. Whether or not the 1902 Treaty is inapplicable the appellants

may test by way of Habeas Corpus, not only the propriety of their detention, but the legality of their disposition (United States v. Curran, 16 Fed. 2d 958, 960; Compare: Lue Chow Yee v. Shaughnessy, (DC N. Y. 1956), 146 Fed. Supp. 3, aff'm'd, 245 Fed. 2d 874; Leng May Wa v. Barber (CCA 9, 1953), 241 Fed. 2d 85; Lew Sing v. Barber (CCA 9, 1954, 215 Fed. 2d 906; Quan v. Brownell, supra).

VI

THE METHODS USED TO ENFORCE THE
1902 TREATY WERE UNLAWFUL, AND
IT WOULD BE CONTRARY TO PUBLIC
POLICY TO APPLY THOSE PROVISIONS
TO APPELLANTS.

One of the most significant features of the government's brief is its plea for preserving the honor and dignity of the United States by upholding the 1902 Treaty. Of course it is necessary to uphold treaties; the question here is, which one? Can it be said, however, that there is less honor and dignity to be served the United States by adhering to the humanitarianism expressed in the 1904 Treaty, than by applying the crass commercialism of the earlier one? Are the concepts of liberty and Democracy to hold out different meanings for the victims of Communist tyranny and Fascist oppression? A world fraught with ideological struggles will pause to hear our answer.

On the other hand, we cannot fail to observe the

government's apparent indifference towards the manner by which appellants were brought within the reach of the 1902 Treaty.

Fortunately, courts will not lend their processes to public officials for the perpetration of illegal law enforcement (McNabb v. United States, 318 U. S. 332, 345; Roberts I., concurring in Sorells v. United States, 287 U. S. 435, 453, at p. 459; People v. Cohen, 44 Cal. 2d 434, 445-446). A judge must ensure a respect for the law in order to promote confidence in the administration of justice, and to preserve the judicial process from contamination (Justice Brandeis, dissenting in Olmstead v. United States, 277 U. S. 438, 471, at p. 485; cf. Delaney v. United States, 199 Fed. 2d 107, 113). In their enforcement of the 1902 Treaty, officials of the United States Immigration Service exceeded the authority entrusted to them by Congress; they violated Mexican sovereignty; and they even failed to confine their enforcement activities within the limits provided by the very treaty they sought to uphold. If the government is permitted, by means of its officers' illicit use of their powers, to effectuate the 1902 Treaty, not only will the government be placed in the role of law-breaker, but other illegal law enforcement practices will be thereby encouraged. There can be no honor and dignity from upholding a treaty where there is none in its enforcement.

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CONCLUSION

For the foregoing reasons, the Order of the District Court denying the Petition for a Writ of Habeas Corpus should be reversed, with directions that said Court make its Order for the return of appellants forthwith to Mexico.

Respectfully submitted,

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PROCEEDINGS OF THE

ANNUAL MEETING OF THE

AMERICAN ASSOCIATION OF

PHYSIOLOGISTS

HELD AT

CHICAGO

DECEMBER 29-31, 1906

AND

THE

1907

IN THE
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APPEAL FROM
UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF CALIFORNIA, CENTRAL DIVISION
HON. THURMOND CLARKE, PRESIDING

APPELLANTS' OPENING BRIEF

FILED

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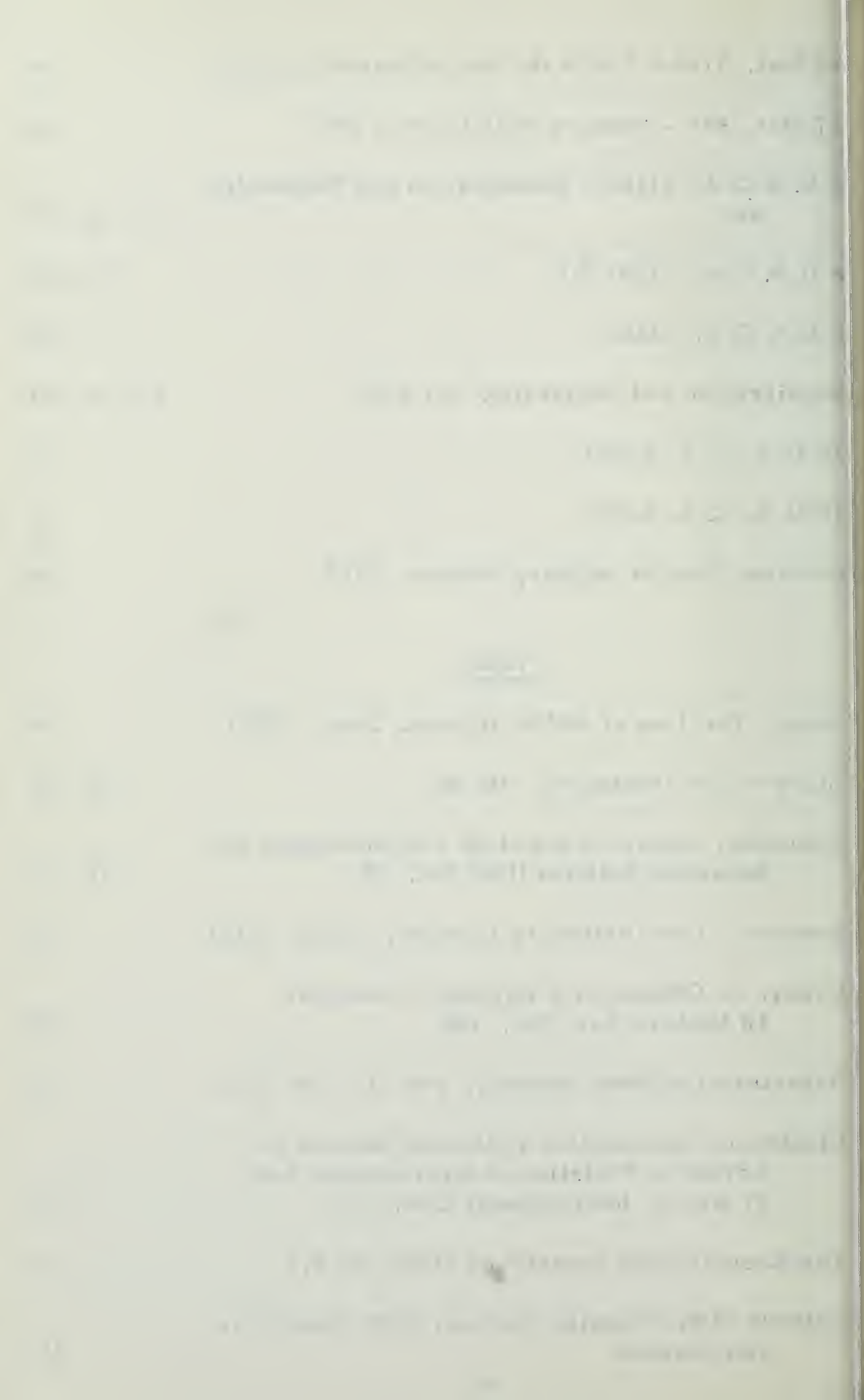
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IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ENRIQUE MEDINA FERNANDEZ, GINAS
IMINEZ NORTES, VICTOR RODRIGUEZ,
MANUEL FERNANDEZ RODRIGUEZ and
AUGUSTIN CABRERA OROZA,

Appellants,

vs.

CHARLES C. HARTMAN, and
ALBERT DEL GUERCIO,

Appellees.

APPELLANTS' OPENING BRIEF

I.

STATEMENT OF THE PLEADINGS AND
FACTS DISCLOSING JURISDICTION

Appellants are nationals of Spain, and seamen in the
Spanish Navy. 1/ On July 8, 1957, a Petition for a Writ of
Habeas Corpus and for Injunction (hereinafter sometimes
referred to as Petition) was filed in their behalf in the United

/ See: Petition for Writ of Habeas Corpus, p. 1.

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States District Court for the Southern District of California,
Central Division, under 28 U. S. C. A. §2241 (c) (3) & (4).
(See Petition, Clk. T. 2.) 2/

Said Petition sought appellants' discharge from the custody of respondent CHARLES C. HARTMAN, Commandant of the Eleventh Naval Base, at San Diego, California, and asked that pending hearing on the Petition, he and his subordinates be enjoined from delivering appellants over to Spanish Naval officers for return to Spain as deserters; and further, for an Order to Show Cause why such Petition should not be granted, and the appellants be discharged from his custody (See: Petition, p. 3; Clk. T. 2).

Custody of appellants was transferred to, and is now in, respondent ALBERT DEL GUERCIO, District Director of Immigration and Naturalization Service, at Los Angeles,

2/ On August 13, 1957, this Court made its order permitting the parties hereto to proceed upon a typewritten record and briefs, and authorizing consideration of the record in its original form.

That record is not available to us here as we prepare this brief, although we do have a copy of the certification of the record by the Clerk of the District Court which contains an index to the Record. Such index, however, refers only to the beginning page of the Record at which cited document is to be found. Accordingly, all references to the pleadings and other documents will be made in this brief by express reference to the particular document cited, and its own page number, and also to the page reference of the Clerk's Transcript as given by the aforementioned index.

Clk. T. refers to the Clerk's Transcript of the Record.

California, pursuant to a minute order of said District Court entered on July 16, 1957 (Clk. T. 23).

On August 1, the District Court entered its Order denying the Petition, dissolving the restraining order, discharging the Order to Show Cause, and directing the delivery of appellants "forthwith" to their respective ships (Order of District Court, dated August 1, 1957, p. 2; Clk. T. 39).

Notice of appeal from said Order was filed August 1, 1957 (Clk. T. 41); and on the same day, the District Court granted a stay of execution for ten days, "pursuant to Rule 27 (1)" (Order Pursuant to Rule 27 (1)).

On August 13, 1957, this Court granted a stay of execution of said judgment pending appeal. Jurisdiction to entertain this appeal is conferred upon this Court by 28 U. S. C. A. §2253.

II.

STATUTES AND TREATIES INVOLVED

The construction and applicability of two treaties between the United States and Spain are at issue.

The respondents rely upon Article XXIV of the TREATY OF 1902 BETWEEN THE UNITED STATES AND SPAIN OF FRIENDSHIP AND GENERAL RELATIONS

33 Stat. 2105, at pp. 2117-2118), 3/ as support for their position and for the judgment of the trial court.

Article XXIV of said Treaty provides as follows:

"The Consuls-General, Consuls, Vice-Consuls and Consular-Agents, of the two countries may respectively cause to be arrested and sent on board or cause to be returned to their own country, such officers, seamen or other persons forming part of the crew of ships of war or merchant vessels of their Nation, who may have deserted in one of the ports of the other.

To this end they shall respectively address the competent national or local authorities in writing, and make request for the return of the deserter and furnish evidence by exhibiting the register, crew list or other official documents of the vessel, or copy or extract therefrom, duly certified, that the persons claimed belonged to said ship's company.

On such application being made, all assistance shall be furnished for the pursuit and arrest of such deserters, who shall even be detained and guarded in the gaols of the country

/ Hereinafter sometimes referred to for convenience as the 1902 Treaty.

pursuant to the requisition and at the expense of the Consuls-General, Consuls, Vice-Consuls or Consular-Agents, until they find an opportunity to send the deserters home.

If, however, no such opportunity shall be had for the space of three months from the day of the arrest, the deserters shall be set at liberty, and shall not again be arrested for the same cause. It is understood that persons who are citizens or subjects of the country within which the demand is made shall be exempted from the provisions of this article.

If the deserter shall have committed any crime or offense in the country within which he is found, he shall not be placed at the disposal of the Consul until after the proper Tribunal having jurisdiction in the case shall have pronounced sentence and such sentence shall have been executed."

Appellants interpose Article III of the EXTRADITION TREATY OF 1904 BETWEEN SPAIN AND THE UNITED STATES, With Protocol of 1907, PROCLAIMED IN 1908 (35 Stat. 1947, 1950, 1955), ^{4/} as precluding their return

^{4/} Hereinafter referred to for convenience as The Extradition Treaty.

parole into the United States temporarily under such conditions as he may prescribe for emergent reasons or for reasons deemed strictly in the public interest any alien applying for admission to the United States, but such parole of such alien shall not be regarded as a admission of the alien and when the purposes of such parole shall, in the opinion of the Attorney General, have been served the alien shall forthwith return or be returned to the custody from which he was paroled and thereafter his case shall continue to be dealt with in the same manner as that of any other applicant for admission to the United States. "

III.

STATEMENT OF THE CASE

A. SUMMARY OF THE FACTS

Appellant MANUEL FERNANDEZ RODRIGUEZ ^{7/} is a young (22 years old) Spanish seaman who was a member of the

^{7/} By stipulation, the testimony of Manuel Rodriguez is deemed the testimony of the other appellants: (R. 41, 42). However, two other appellants testified briefly, and where their statements are believed relevant and useful, reference to them will be made in an appropriate footnote.

crew of the Spanish destroyer, ALMIRANTE FERRANDIZ

(R. 7). 8/

In his household in Spain, Manuel had learned something of freedom, but the price had been heavy. Two of his brothers had been killed fighting for the Loyalist cause during the Civil War, while a third was forced into exile, and now lives in Chile (R. 16). 9/

As a young boy, after the war, Manuel, and his family, had been compelled to witness the execution of Loyalists and their sympathizers, for those who failed to do so were "called 'Reds' and they were beaten and . . . at times killed", (R. 22).

After the war, the only political party permitted in Spain was, and still is, the Falange.^{10/} Membership in the Falange was made virtually a pre-requisite for those seeking higher education (R. 45-48), or even a decent job (R. 19-21, 46). Without Falangist connections, one was able to obtain only the most arduous labor, and that at reduced wages (R. 19-20, 54). Criticism of conditions could lead to losing one's job (R. 54) or punishment infinitely worse (R. 49, 55). Moreover, the

8/ R. refers to the Reporter's Transcript of the oral proceedings had in the District Court below. The number refers to the page on which the reference may be found.

9/ Ginas Jiminez Nortes (suing as Ginas Jiminez Martinez) testified that his father and uncle had been jailed several times during the war because of their refusal to take up arms for Franco (R. 48).

10/ See appendix "A" - J.

workingman had no union to protect him, save that which "cooperated" with Franco (R. 20, 21).

And so, at fourteen, Manuel joined the Falange (R. 18). ^{11/}
But a year later he quit the Party because he could no longer suffer its principles, and because "they were the ones who killed my brothers" (R. 18). When he stopped attending Falangist classes, he was fired from his job (R. 19). ^{12/}
After that, he could only find menial jobs at low wages.

In about 1955, Manuel entered the naval service (R. 28). ^{13/} Early this year, he was assigned to a crew that was being sent to San Francisco, California, for the purpose of taking custody of two destroyers which our government was giving to Spain (R. 37; see also Respondent's Exhibits A and

^{11/} So did appellant Nortes, for similar reasons (R. 46, 47). Joining the Falange meant wearing a uniform, attending special Falangist classes, and taking an oath to support - not the government - but Franco (R. 20, 46, 47).

^{12/} Nortes testified that he suffered the same fate, and also encountered difficulties at the University when he was made to repeat classes on that account.

^{13/} Nortes stated that he joined the Navy with the idea of deserting in a free country, because there was no future in Spain for those who "want to get married and have children" (R. 53).

Appellant Enrique Medina Fernandez testified that he entered the Navy because he could not support his sisters and parents any other way (R. 62)

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B). At that point, MANUEL vowed to somehow utilize this opportunity to escape from Spain (R. 32).

En route to San Francisco, he made an abortive attempt to desert in Panama, which country he believed had not recognized Franco Spain (R. 39). Unable to find other members of the crew who had deserted before him, he abandoned that effort, and returned to the ship (R. 39).

Thus, on March 17, 1957, MANUEL, and the other appellants, arrived with the crew in San Francisco (R. 30, 63), and began training with the United States Navy for the purpose of learning how to use the destroyers (R. 52). During this period, MANUEL was given several shore leaves of extended duration, but he made no effort to escape then (R. 38), probably in the hope that a more favorable opportunity would present itself (R. 32). 14/

Such an opportunity came in June, when the training of the ships' crew shifted to San Diego (R. 28). There, on

14/ Nortes testified on cross examination:

"I had several opportunities in San Francisco, but since my intention was to go into --- was to desert in Mexico, I did not want to take the opportunities there", (R. 53).

Appellant Fernandez was granted short leave about fifteen times, but made no attempt to desert in the United States, (R. 57)

June 4, MANUEL and a shipmate, the appellant, OROZA, were granted a four hour shore leave, commencing at 6:00 P. M. and terminating at 11:00 P. M. (R. 29). Upon leaving the ship, they proceeded at once for Mexico, and crossed the border into Tijuana, Baja California, at approximately 8:30 P. M., the same evening (R. 8). 15/ Fifteen days later, the two boys surrendered to the local Mexican police, and asked for political asylum (R. 9, 44). It may be assumed that the other three appellants did likewise. 16/

But appellants were far from free; their troubles had only begun. While in the custody of Mexican authorities, appellants were paid a visit by the Captain of the ALMIRANTE FERRANDIZ, and by a petty officer of the United States Navy,

15/ Appellants Fernandez and Nortes were given shore leave commencing at 6:00 P. M., June 21, and terminating at 1:00 A. M., June 22; and on June 16, Victor Rodriguez was granted shore leave commencing at 9:00 P. M. that date, and terminating at 7:00 A. M. the following morning (See: Answer, para. II (7), at p. 3, Clk. Tr. 24). The evidence is uncontroverted that each appellant entered Mexico before his shore leave had expired (R. 44, 56).

16/ See stipulation of counsel whereby Manuel's testimony is deemed that of the others (R. 41, 42). See also, testimony of appellant Fernandez (R. 61), and of appellant Nortes (R. 50).

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who accompanied him (R. 91, 92). 17/ The Captain asked appellants to return to their ships voluntarily, holding out the promise of reward if they did so (R. 14). 18/ Appellants refused (R. 15). For they feared that return to Spain meant a long term in prison - and possibly death (R. 24, 55, 62). 19/

On July 5, 1957, appellants were paroled into the United States by order of respondent DEL GUERCIO, who was purporting to act under the provisions of §212(d)(5) of the Immigration and Nationality Act (8 U. S. C. A. §1182 (d)(5)); and thereupon, they were delivered into the custody of the respondent HARTMAN for return to their respective ships (See: Order of Parole, Plaintiff's Exhibit #1). 20/

17/ As a "guide", according to the government, presumably because there are no diplomatic relations between Spain and Mexico (See: Answer to Amendment to Petition For Writ of Habeas Corpus, para. II (4), at p. 2, line 17 (Clk. T. 24)).

18/ Forgiveness and a fifteen day shore leave in San Diego, according to Manuel's testimony.

19/ It would appear that while in Mexico, appellants had publicly criticized the Franco regime, and these comments had been published in the Mexican press (See: R. 23, 61). This led Fernandez to express the --

"... fear that they would put us in jail or that they would kill us because of having spoken against the government" (R. 62).

That such fear was not groundless, see Appendix "A" - E.

20/ The Order of Parole recites that appellants made application for admission into the United States. On the reverse side of the Order appears the signature of appellant Enrique Medina Fernandez, acknowledging that he has read
(Continued)

On July 8, 1957, the United States District Judge, HON. THURMOND C. CLARKE, issued his Order directing respondent HARTMAN to show cause why the petition for Writ of Habeas Corpus should not be granted and the appellants discharged from his custody, and further ordering that said respondent and his subordinates be enjoined, pending hearing on the Petition, from delivering appellants to their ships, or removing them from the Court's jurisdiction (See: Order to Show Cause and Restraining Order; Clk. Tr. 6).

The hearing upon the Order to Show Cause and the Petition was held on July 19 and 23, 1957, concluding on the latter date with argument by Counsel (See: R. 172, 96-170). At the commencement of the proceedings, Mr. Philip Newman, an attorney, representing the government of

20/ (Continued:) and understands the conditions of parole, and, inter alia, agreeing to abide by its terms. Fernandez testified, however, that he did not know what he was being asked to sign, that he neither read nor understood English, and that he had made no request or application for return to the United States (R. 59-60).

No application for admission as such was offered by the government; and as a matter of fact, the appellants denied having made any, and insisted that their return to the United States was involuntary and against their will (R. 24, 59, 60).

None of this evidence was controverted or challenged by the government.

Mexico, appeared before the Court, and informed the Court that Mexico considered appellants "as people who could qualify as political refugees", and that upon their application at any port of entry, "the Mexican government will admit these five subjects as political refugees" (R. 4).

Thereafter, on August 1, 1957, the District Court made its Order adverse to appellants as aforescribed, and this appeal followed.

B.

QUESTIONS INVOLVED

The respondents take the position that they are acting under the provisions of Article XXIV of the 1902 Treaty with Spain, and that by its terms, they are under a duty to seize and detain seamen from Spanish warships who desert in our ports, and return them to their superiors upon demand; 21/ that appellants fell within this category, and that irrespective of any impropriety in their seizure or arrest, the Treaty affords a legal basis for their detention (See: Respondents' Answer and Return; also, argument of U.S. Attorney, at R. 133-149, 165-170).

21/ It should be noted that demand in the form prescribed by the 1902 Treaty was not made until July 12, some four days after the Order to Show Cause and Restraining Order had been issued (See: Respondent's Exhibits "C", "D", "E", & "F"). Moreover, it is doubtful that a valid demand was made even then, for the Spanish Consul submitted the crew list required by Article XXIV to the trial judge, rather than to a "competent officer," i. e. an official of the executive branch of government (See: Exhibit F; R. 73-85)

respondents had the authority or duty to apprehend appellants for delivery to their ships is wholly without support in the evidence, and is contrary to law.

3. The Order of the District Court, dated August 1, 1957 (Clk. Tr. 39) denying appellants' petition for Writ of Habeas Corpus and for Injunction, Dissolving the Restraining Order, discharging the Order to Show Cause, and directing their return to their respective ships, is wholly unsupported by the evidence, and is manifestly contrary to law, for the following reasons:

- a) The Court failed and refused to find that appellants had committed offense of a political character;
- b) The Court failed and refused to conclude that the Extradition Treaty of 1904 with Spain was applicable, and barred appellants' surrender to the Spanish authorities;
- c) The Court failed and refused to find and conclude that respondents had no jurisdiction over appellants in that they were not within the United States, and amenable for such delivery to Spanish authorities.
- d) The Court failed and refused to find and conclude that respondents lacked authority to seize and detain appellants from the territory of a foreign country.
- e) The Court failed and refused to find that the 1902 Treaty was inapplicable to the case at bar for failure of the Spanish authorities to comply therewith.

"... for the pursuit and arrest of such deserters ...", and for their detention. "Such deserters" refers to "seamen ... forming part of the crew of ships of war ... of their nation, who may have deserted in one of the ports of the other."

The applicability of Article XXIV, therefore, and hence, the authority for seizing and detaining appellants, turns upon whether or not they deserted "in one of the ports of the (United States)."

It is submitted that the phrase just cited should be construed literally, and we believe there is a sound historical and legal basis for such approach.

In August, 1901, six Spanish seamen deserted their ships in New Orleans, Louisiana. Local authorities refused to aid the Spanish master in their capture. As a result of this incident, the Minister Plenipotentiary of Spain, the Duke de Arcos, protested to the then Secretary of State, Mr. Hay, in a note dated September 25, 1901, containing the following pertinent language:

"The Consul appeared before the competent authorities asking their aid in arresting the sailor deserters, as customary in all ports; but the said authorities refused to grant the request of the Consul, on the ground that there was no existing treaty between Spain and the United States that

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qualifications thereto. Had the parties intended that desertion from the military service - as well as desertion from the ship - was to be made subject to the provisions of Article XXIV, they would have expressly so stated, as they did in the original draft of Article III of the Extradition Treaty of 1902 (and subsequently discarded in the Protocol of 1907), 21-a/ While it is quite likely that Spain regards the appellants as military deserters, neither these courts nor the respondents could be called upon - under Article XXIV - to enforce what is in reality the law of a foreign government.

Tucker v. Alexandroff, 183 U.S. 424, 433, 434.

The offense of desertion is variously defined as:

1. " ... a soldier or sailor who absents himself without leave with the intention of not returning. "

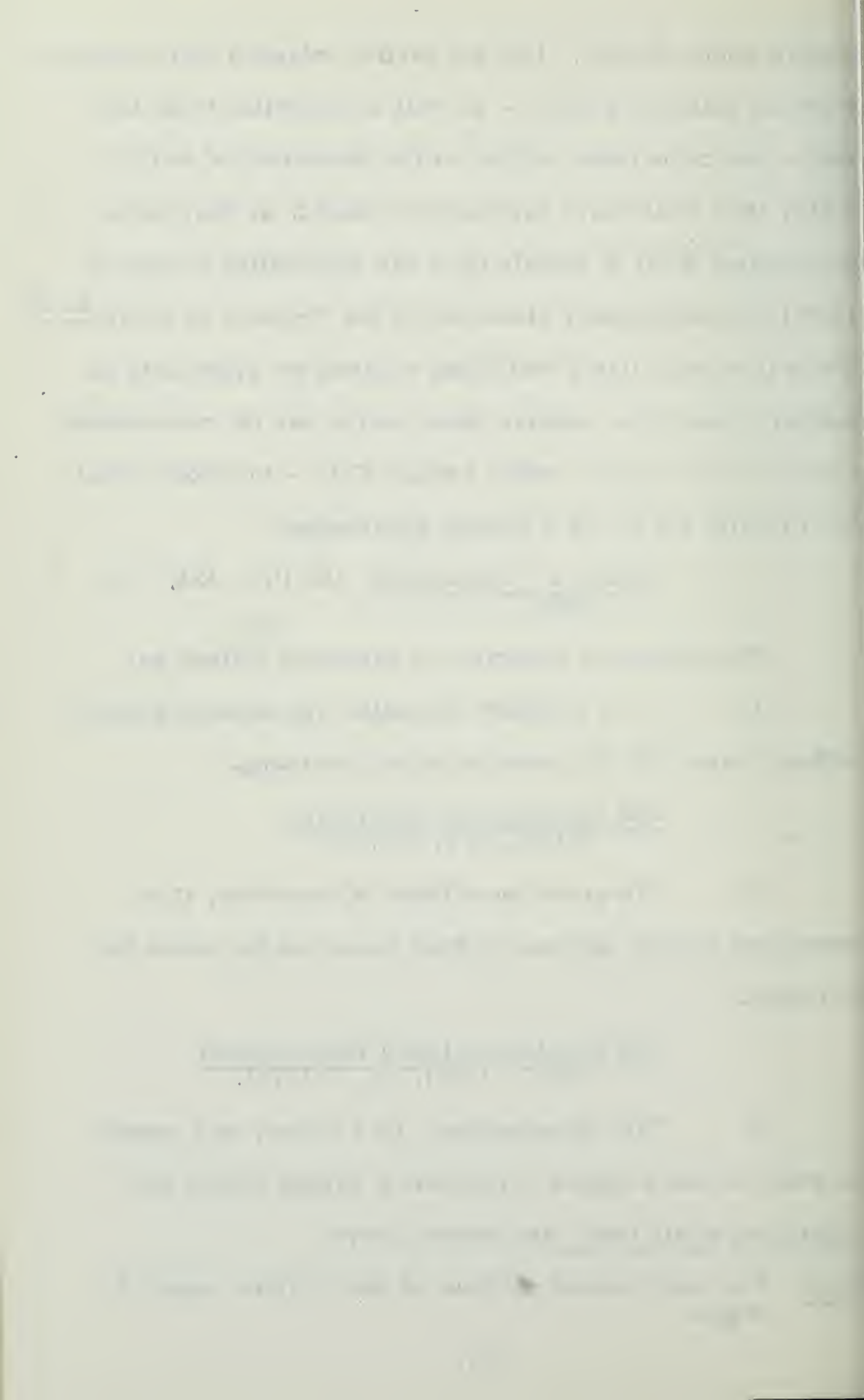
The Encyclopedia Americana
(1954, N. Y.), p. 8

2. "To prove the offense of desertion, it is necessary to show absence without leave and the intent not to return. "

The New International Encyclopedia
(U. S., 1924), pp. 713-714.

3. "The abandonment, by a sailor, of a vessel in which he had engaged to perform a voyage before the expiration of his time, and without leave. "

21-a/ See underscored portions of that Article, page 19, supra.



4. "By desertion, in the maritime law, is meant

not a mere unauthorized absence from the ship without leave, but an unauthorized absence from the ship, with an intent not to return to her service ..."

Black's Law Dictionary, (4th Ed.).

5. "... a deserter is one who is absent without

leave and with a manifest intention not to return ..."

Reed v. United States, 252 Fed. 21

6. "The crime of desertion requires two elements:

(1) absence without authority, and (2) intent to remain away permanently. "

Griffen v. United States, 115 Fed. Supp. 509
(Rev'd on other grounds, 216 Fed. 2d 217).

7. "A quitting the ship and her service, not only

without leave and against the duty of the party, but with an intent not again to return to the ship's duty. "

Quoted with approval in Winthrop's
Military Law and Precedents (2d Ed. 1920),
FN. 24, at p. 637.

8. "(a) Any member of the armed forces of the

United States who -

(1) Without proper authority goes or remains absent from his place of service, organization, or place of duty with intent to remain away therefrom permanently ..."

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It will be seen from these diverse authorities that the offense of desertion requires the presence of two elements, to wit: 1) absence from an assigned station, ship or duty without authority, and 2) an intent to remain away permanently. Unless both of these elements are present, there is no desertion.

In the case at bar, the question is not so much whether desertion occurred as it is when and where. Respondents admit that each appellant had shore leave of four or more hours (Answer, Para II (7), p. 3; Clk. Tr. 24). The evidence is overwhelming and unrefuted that each appellant crossed the border into Mexico before his leave expired (See p. 11, supra). Even if we assume that each appellant left his ship with the intent to desert in Mexico - an assumption not unwarranted by the evidence - the offense of desertion could not have occurred until the expiration of their respective shore leaves; in other words, in Mexico. By definition, desertion requires an overt act as well as the intention to commit it. 21-b/ Thus according to Winthrop's Military Law and Precedents

21-b/ "[The rules of law], whether civil or even criminal, never inflict penalties upon mere internal feeling, when it has produced no result in external conduct." (Kenny, Outlines of Criminal Law [15th Ed., Camb., 1936], p. 40).

E.

EVEN IF THE APPELLANTS DID DESERT,
THEIR OFFENSE UPON THE FACTS AT
BAR WAS OF A POLITICAL NATURE, AND
THEREFORE, UNDER THE EXTRADITION
TREATY OF 1904, IS NON-EXTRADICTABLE.

1.

THE ISSUE

As exemplified by the case of these five appellants, the struggle for liberty is not confined to countries behind the "iron curtain". Nor, unfortunately, is freedom necessarily guaranteed to those whose rulers claim our friendship. We, of course, are not here to pass judgment upon governments, or the institutions by which they rule, but rather to determine the fate of a few men who dare to love freedom enough to risk their lives in search of it. It is natural enough that we examine into the sincerity of its pursuers; yet, liberty is not a right to be enjoyed only by those who pursue it with clean hands. The nature of despotism forbids such a narrow view.

Though appellants stressed the political character of their offense, and urged the Extradition Treaty of 1904 as a bar to their detention and surrender to Spain, the trial court's order fails even to note the claim. In this defect, and in the conclusion that respondents have jurisdiction over the offense at bar, the Court's order is in error.

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THE EXTRADITION TREATY IS
APPLICABLE TO THE CASE AT BAR

Once the sovereign has agreed to delimit its power by treaty, the scope of that power, and the manner in which it is exercised is defined by the terms prescribed in such treaty.

Valentine v. United States, 299 U. S. 5, 9.

Cook v. United States, 288 U. S. 102.

United States v. Ferris, 19 Fed. 2d 925.

Karadzole v. Artukovic, (CCA 9), Case No. 15217, June 24, 1957 (Unreported)

"A power to seize for the infraction of a law is derived from the sovereign, and must be exercised, it would seem, within those limits which circumscribe the sovereign power . . . "

(Rose v. Himley, 4 Cranch 241, 279.)

Since the power of respondents to seize appellants as deserters, and deliver them to their ships, is derived from a treaty, it is thereby subject to such limitations as the treaty signatories may put upon it. Those limitations, however, need not be in the treaty granting the power, but may be contained elsewhere (cf. Johnson v. Browne, 205 U. S. 309, 320). Thus, the authority conferred by Article XXIV of the 1902 Treaty has been circumscribed by a Congressional statute (§16 of the Act of March 4, 1915, 38 Stat. 1164, 1184).

the following is a list of the names of the persons who have been elected to the office of President of the Institute for the year 1910.

1910. — President, Sir John Lubbock, Bart.

Vice-President, Mr. J. H. R. Murray.

President Elect, Mr. J. H. R. Murray.

President Elect, Mr. J. H. R. Murray.

President Elect, Mr. J. H. R. Murray.

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Moreover, we submit that Article XXIV is further delimited by the terms of Article III of the more recent Extradition Treaty of 1904. 22/

The crucial language of Article III is to be found in the phrase:

"The provisions of this Convention shall not import claim of extradition for any crime or offence of a political character, nor for acts connected with such crimes or offences . . . "

"The provisions of this Convention" enumerate a long list of extradictable crimes, and prescribe the manner by which such extradition shall be effected. Yet, in Article III, the term "import" is used, as if to acknowledge the existence of a tradition or policy 23/ whereby political asylum is afforded as a matter of course. But if the context of the term is enlarged to include the words "shall not import claim of extradition," its sense is likewise magnified, so as to incorporate a broader definition, e. g. : "to bear or carry with it . . . " (Webster's Collegiate Dictionary, 5th Ed. ; see also

22/ The provisions of which have been set forth at p. supra.

23/ Import in this sense is defined in The Oxford Universal Dictionary, 3 Ed., Revised with Addenda, as:

"5. to involve; to imply 1529; to convey in its meaning; to signify, denote 1533; to bear as its purport; to express, state, make known . . . "

The Oxford Universal Dictionary, supra, Footnote 23.) By substituting this definition for the word "import", Article III might read:

"The provisions of this Convention shall not carry with it [any] claim of extradition [for political offences] . . . "

It is evident, then, that the manifest objective and meaning of Article III is to authorize extradition only of persons accused of ordinary crimes, it being understood between the parties that political offenses are not extraditable.

While it is true that Article III employs the term "extradition", that fact does not put appellants beyond its reach. Extradition means simply to surrender an accused to the demanding power (See: Black's Law Dictionary, 3rd Ed). But as we have pointed out, Article III expresses a criterion of general conduct and relations between the parties, rather than being limited in its operation and effect to the twenty-two ordinary crimes enumerated in Article II of the Convention. Actually, the only significant difference between Article XXIV of the 1902 Treaty, and the Extradition Treaty is the procedure by which the surrender is to be accomplished. Article XXIV calls for a summary procedure because time is of the essence. Yet, the result is virtually the same; the offender is delivered to the demanding sovereign.

It remains, therefore, only to consider whether

appellants' desertion is an offense of a political character.
If so, their detention is unlawful.

3.

APPELLANTS' DESERTION WAS AN ACT
OF A POLITICAL CHARACTER

As one writer soberly observed:

"In an age when one party only is permitted
in a State, perhaps the only remaining method
of active political protest may lie in withdrawing
from that State and living elsewhere." 24/

His point aptly suggests the difficulties inherent in
attempting a definition of offenses of a political nature. None
could possibly satisfy all of the acts which oppression justifies,
or which humanitarianism condones. A chance remark, the
purchase of black market coffee, possession of a short-wave
radio -- simple items which we take for granted -- may give
impetus for flight elsewhere. In weighing the political charac-
ter of the escape of seven Polish sailors to England, Lord
Goddard, C. I., stated:

" . . . it is necessary, if only for reasons
of humanity, to give a wider and more
generous meaning to the words we are now

24/ Denny, An Offense Of a Political Character, 18
Modern Law Review 380, 384.

the following: (1) the patient's condition; (2) the patient's wishes; (3) the patient's family; (4) the patient's community; (5) the patient's country.

The following are the principles of the code:

1. The patient's condition is the primary consideration.

2. The patient's wishes are the primary consideration.

3. The patient's family is the primary consideration.

4. The patient's community is the primary consideration.

5. The patient's country is the primary consideration.

6. The patient's condition is the primary consideration.

7. The patient's wishes are the primary consideration.

8. The patient's family is the primary consideration.

9. The patient's community is the primary consideration.

10. The patient's country is the primary consideration.

11. The patient's condition is the primary consideration.

12. The patient's wishes are the primary consideration.

13. The patient's family is the primary consideration.

14. The patient's community is the primary consideration.

15. The patient's country is the primary consideration.

16. The patient's condition is the primary consideration.

17. The patient's wishes are the primary consideration.

18. The patient's family is the primary consideration.

19. The patient's community is the primary consideration.

20. The patient's country is the primary consideration.

21. The patient's condition is the primary consideration.

22. The patient's wishes are the primary consideration.

construing . . . " 25/

Historically, the United States has treated flight from oppression as a political act, with the result that we have been enriched by the contributions of such political refugees as Toscanini, Sikorsky, Undset, Waksman, Robert Wagner, Sr., Rachmaninoff, Shurz, Pulitzer, Stravinsky, Lotte Lehman, Einstein and Frankfurter.

Our humanitarian policy toward political refugees is frequently reflected in our statutes, 26/ and only recently, led to the acceptance by the United States of more than 31,000 Hungarian refugees, twenty percent of all those who escaped Communist oppression in their homeland. 27/

But flight from rebellion and civil strife is not necessarily the earmark of a political refugee. (Compare, for example, the plight of the Jews in Nazi Germany.) Rather, the United States accepts the view that they "are persons who

25/ Ex Parte Kolczynski, 1954, 2 Weekly Law Reports 116 (1955); 1 All. E. R. 31; quoted with approval by this Court in Karadzole v. Artukovic (CCA 9), No. 15,217, decided June 24, 1957 (unreported).

26/ See: Refugee Relief Act of 1953, 67 Stat. 400 (50 App. §1971), as amended by Act of August 31, 1954, 68 Stat. 1044. Compare also: §243(h) of the Immigration and Nationality Act (8 U. S. C. A. §1253(h)).

27/ The Department of State Bulletin (May 6, 1957), Vol. 36, No. 932, at p. 721.

fear return to their countries of origin, " 28/ and has accordingly announced :

"The United States is firmly opposed to forced repatriation in any form whether by direct steps or indirect steps which might tend to accomplish this. " 29/

On the fifth anniversary of the United States' Escapee Program, Robert S. McCollum, head of the Office of Refugee and Migration Affairs (State Department), warned:

" . . . as long as oppressive dictatorships exist, as long as basic individual freedoms are denied, there will be people who flee to seek better lives and thereby create new refugee problems . . .

"Pleased as we may be about our Country's part in accepting Hungarian escapees,

28/ Speech by Jacob Blaustein, United States Representative to the General Assembly, delivered in Committee relating to the Report of the High Commissioner For Refugees. Bulletin, op.cit. Vol. 33, p. 628, at p. 631. In approving the definition of political refugee established by the United Nations Mandate, Mr. Blaustein stated:

"These refugees are people who had to leave their own countries of residence through no fault of their own, but because of war, revolution, and oppression -- conditions beyond their control. "

ibid, at p. 628.

29/ Blaustein, op.cit. p. 634.

who achieved, and still holds, his power by force and violence; that there is religious and political persecution in Spain; that the Spanish press is completely controlled by Franco, and political dissent is ruthlessly suppressed; that only one political party, The Falange, is permitted to exist, and this organization dominates the whole political and economic life of the nation; and that there are persons who have been promised amnesty by Franco, only to be executed upon their return to Spain. 33/

This, then is why MANUEL RODRIGUEZ --

" . . . was fleeing the Franco regime." (R. 15);

why GINAS JIMINEZ NORTES --

" . . . was looking for a country where I

could be free and I could do whatever my

capacity and my reasoning decided for me" (R. 45);

and why ENRIQUE FERNANDEZ had --

"A fear that they would put us in jail or

that they would kill us because of having

spoken against the government" (R. 62).

It is difficult to conceive of a more purely political act than flight from Franco tyranny. 34/ That it may be

33/ See Appendix "A", containing a digest of leading periodical and newspaper articles describing the political events which give support to this portrayal of Spain.

34/ Mexico regards appellants as political refugees, and is willing to accept them as such (R. 4). (Continued)

characterized by the demanding State as a statutory crime is to be expected. In the Kolczynski case (supra, fn. 25), the theft of a ship, and the wounding of an officer, by seven Polish sailors escaping to England were treated as political crimes, and hence, non-extraditable. Karadzole v. Artukovic (CCA 9), No. 15,217 (unreported) (June 24, 1957), involved a Yugoslav accused of war atrocities by his government; yet, this Court held genocide a political act which barred his repatriation.

There is no sound reason, therefore, why desertion from a ship, when prompted by bona fide political motives, cannot be regarded as a political offense. Indeed, the United States has extended assylum to deserters. Thus, in 1955, the State Department rejected a demand by Czechoslovakia for the return of a border guard who had fled into the American zone "for political reasons". 35/

34/ (Continued) And, according to one source, France has admitted over 200,000 Spanish refugees on political grounds. Weis, The International Protection of Refugees, 48 Am. J., Int'l Law 193 (1954).

See also: United States ex rel Watts v. Shaughnessy (D. C., S. D., N. Y.) 107 Fed. Supp. 613, where Judge Irving Kaufman stayed the deportation of an alien to Spain on grounds that he might be persecuted there.

35/ In its note, the State Department declared that it would not violate its traditional practice of refusing to return to a foreign jurisdiction persons who have left it for political reasons.

"Under a system of political oppression denying its citizens the right to choose freedom, violence and tragedy are bound to occur."

Bulletin, op.cit. Vol. 32, pp.736-737 (dated May 2, 1955).

Again, in 1956, the United States extended political sanctuary to six Russian seamen who had deserted their ships in Formosa. 36/

It has even been our policy during, and since, World War II, to refuse, out of justice and decency, to repatriate enemy deserters. 37/ Indeed, it is common knowledge that our government encourages those who chafe under totalitarian systems to desert their fate at their earliest opportunity; and large rewards have been offered to, and citizenship conferred upon, refugees who escape with military equipment. 38/

As appellant Nortes put it so eloquently:

"I wasn't thinking of deserting. I was thinking of leaving the Franco regime and go to a free country where a man could use his freedom." (R. 50).

Manifestly, appellants' desertion was an offense of a political character, and consequently, the respondents are without authority or jurisdiction to return them to their ships.

See: Karadzols v. Artukovic, supra.

36/ See: "The Episode of the Russian Seamen", Report of the Sub-Committee of the Judiciary to Investigate the Administration of the Internal Security Act and other Internal Security Laws (May 24, 1956), 84th Cong., 2nd Session.

37/ Garcia-Mora, International Law and Asylum as a Human Right, (Public Affairs Press, 1956), p. 105.

38/ New York Times, August 5, September 21-22, 1953.

ASSUMING THE APPLICABILITY OTHERWISE OF THE 1902 TREATY, RESPONDENTS ARE WITHOUT JURISDICTION TO DELIVER APPELLANTS TO THEIR SHIPS.

1.

RESPONDENTS DID NOT ACQUIRE JURISDICTION OVER APPELLANTS WHEN THEY PAROLED THEM INTO THE UNITED STATES FOR THE PURPOSE OF DELIVERY TO THE SPANISH AUTHORITIES SINCE SUCH PURPOSE WAS PROHIBITED BY LAW.

The District Court ordered the delivery of appellants to their ships, presumably pursuant to the 1902 Treaty. ^{39/} Such Order was error because the Court had no jurisdiction to make it, and the respondents are without authority to comply with it.

The evidence shows that appellants were paroled into the United States from Mexico pursuant to §212(d)(5) of the Immigration and Nationality Act (8 U. S. C. A. §1282(d)(5)). ^{40/}

That statute empowers the Attorney General in his discretion to parole into the United States for emergent reasons or for reasons deemed strictly in the public interest any alien applying for admission. The statute expressly

^{39/} See: Order Denying Petition, etc. (Clk. T. 39).

^{40/} Petitioners' Exhibit 1. The statutory provisions are set forth in full at pp. 6-7, supra.

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provides, however, that such parole shall not constitute an admission into the United States, and that when the purposes of the parole have been served, "The alien shall forthwith return or be returned to the custody from which he was paroled . . . "

It is apparent that the Attorney General has the discretion to determine whether the statutory grounds for parole are met by the applicant. It is also true that the Attorney General may delegate this authority to his subordinates, although obviously the latter cannot exceed the powers which have been conferred upon him by Congress. In the case at bar, Respondent Del Guercio has exercised a power which he claims was granted to his superior, the Attorney General. This assertion requires examination.

Whatever discretionary power §212(d)(5) of the Immigration Act confers upon the Attorney General, recent United States Supreme Court decisions involving aliens under his supervision and control make it clear that such discretion must be exercised within the confines of Congressional intent.

United States v. Witkovich, 353 U.S. 194,
1 L. Ed. 2d 765.

Barton v. Sentner, 353 U.S. 963, 1 L. Ed. 2d
901, aff'm'g. 145 Fed. Supp. 569.

See also: United States v. Zucca, 351 U.S. 91.

The legislative history of §212(d)(5) reveals -- if the statutory language does not -- that the sort of "emergent

reasons" or "public interest" which Congress had in mind were those which could be satisfied or performed wholly within the territorial limits of the United States. 41/

This view is buttressed by the express legislative mandate requiring the alien "be returned to the custody from which he was paroled . . . ". In fact, this is one of the terms and conditions of the Parole Order. 42/

Once, of course, the Attorney General loses control or custody of the alien, he is unable to comply with Congress' command. Manifestly, this is bound to be the result if appellants are surrendered to Spanish jurisdiction.

It was never contemplated by Congress that §212(d)(5) should serve the interests of a foreign power; but it is quite apparent from the terms and conditions of the Parole Order (line (h), p. 2), that Respondent Del Guercio had precisely that intention when he paroled appellants into the United States. Moreover, the Order of the District Court purports to carry out this purpose, and to compel performance of an act which patently transgresses the legislative scheme of the Statute.

Since the delivery of appellants cannot be accomplished

41/ U. S. Code Congressional and Administrative News (1952), Vol. 2, at p. 1706. For example, where an alien requires immediate medical attention before inspection can be made; or where the alien is desired as a witness for prosecution.

42/ See Petitioners' Exhibit 1, line (b).

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without doing violence to the statute under which respondents purport to act, a Writ of Habeas Corpus will lie, even though appellants' detention may be otherwise valid.

United States v. Curran, 16 Fed. 2d 958, 960
(and cases cited thereat).

In fact, the absence of a lawful basis for paroling appellants into the United States constitutes a fatal jurisdictional defect which renders the seizure and detention of appellants void ab initio. 43/

See: Mahler v. Eby, 265 U. S. 32.

See also: United States v. Zucca, supra.

43/ A condition precedent to the issuance of an order of parole is an application for admission. (§212(d)(5) of Immigration Act; 8 U. S. C. A. §1182(d)(5)). The failure to make such an application would vitiate the Order of Parole ab initio (United States v. Zucca, 351 U. S. 91; Mahler v. Eby, 264 U. S. 32). While the Order of Parole recites that application was made, the evidence is to the contrary. Appellants repeatedly denied such application was ever made, and insisted they were forced into the United States against their will (R. 24, 60). Moreover, the Parole Order was not explained to Appellant Fernandez, who signed it, and he could not read it because he was unable to understand English (R. 59, 60). None of this testimony was ever denied or challenged by the government. And since the appellants had no intention of deserting in the United States, their claims are entirely consistent with their prior conduct. This would therefore constitute an additional reason why appellants' detention is illegal.

IN CONTEMPLATION OF LAW, APPELLANTS ARE IN MEXICO, AND ANY EFFORT BY RESPONDENTS TO EFFECT THEIR RETURN TO THEIR SHIPS WOULD VIOLATE MEXICAN SOVEREIGNTY, AND THEREFORE MUST FAIL FOR WANT OF JURISDICTION.

But whether or not their detention is valid, it is clear that appellants cannot be delivered to the Spanish authorities because they are not within the United States.

§212(d)(5) specifically states that the parole of aliens into the United States "shall not be regarded" as an entry. They are, as it were, outside the gates, knocking for admittance.

Ekiu v. United States, 142 U.S. 651.

United States ex rel Mezei v. Shaughnessy,
345 U.S. 206, 213.

Indeed, this Court has held that aliens in the legal posture of appellants are ineligible for discretionary relief under the physical persecution section of the Immigration (8 U.S.C.A. §1253(h)), for the precise reason that they are not within the United States. 44/

44/ If, on the other hand, the Attorney General has authority to surrender these appellants into Spanish hands, notwithstanding §212(d)(5), he is then under a correlative legal duty to entertain their claims for discretionary relief under §243(h) of the Immigration Act (8 U.S.C.A. §1253(h)). Quan v. Brownell (CADC), 26 L.W. 2025, dated July 16, 1957; NG Lin Chong v. McGrath (CADC), 202 Fed.2d 316. This the Attorney General has not done, and therefore, in the event the Court fails to sustain the other of appellants' claims (continued)

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Lew Sing v. Barber (CCA 9), 215 Fed. 2d 906;
Cert. granted, 348 U. S. 910;
judgment vacated, and petition ordered
dismissed as moot, 350 U. S. 898.

Leng May Ma v. Barber (CCA 9), 241 Fed. 2d
85; cert. granted, #916, June 3, 1957
(17 CCH 8040).

Appellants had no such documents, so that to pull them into the United States via Article XXIV would place the 1902 Treaty in a status superior to that of the Federal law and Federal Constitution. Plainly, a treaty cannot have such effect.

See: Head Money Cases, 112 U. S. 580, 599.

More than that, however, Article XXIV cannot afford a jurisdictional basis for the surrender of appellants because their juridical persons are in Mexico. Since the 1902 Treaty is bilateral -- not multilateral -- their delivery to Spain would give the Treaty an extra-territorial effect. From the doctrine that the territory of a sovereign state is absolutely inviolable, ^{45/} it is axiomatic that the legal reach of a treaty is confined to the

44/ Continued: herein, an order of the Court enjoining delivery of appellants to their ships until he so exercises his discretion would be proper and serve the ends of justice. See: Mahler v. Eby, supra; United States v. Curran, supra.

45/ "The duty to respect the territorial supremacy of a foreign State must prevent a State from performing acts, which although they are according to its personal supremacy within its competence, would violate the territorial supremacy of this foreign State. A State must perform no acts of sovereignty in the territory of another State."

Oppenheim, International Law, Vol. I, p. 295.

territory of the contracting nations.

In any event, the United States certainly cannot transgress the territorial sovereignty of a country with whom it is at peace, let alone do so as an agent of another nation. 46/

If the United States is entitled to assert extra-territorial rights in Mexico looking toward the return of a fugitive, it would only be by virtue of an extradition treaty with such country, or by comity.

See: Valentine v. United States, 299 U.S. 5, 9.

Such a treaty provides the exclusive mode for the recovery of a fugitive, and a demanding State lacks power to resort to other means to effect his capture.

Cook v. United States, 288 U.S. 102, 120-122.

United States v. Ferris, 19 Fed.2d 925.

Collier v. Vaccaro, 51 Fed.2d 17.

It so happens that an extradition treaty exists between Mexico and the United States which definitively establishes the procedures to be followed for the recovery of fugitives. 47/

46/ In United States v. Curtis-Wright, 299 U.S. 304, the Supreme Court declared:

"Neither the Constitution nor the Laws passed in pursuance of it have any force in foreign territory unless in respect of citizens of the United States, and operations of the nation in such territory must be governed by treaties, international understandings and compacts and the principles of International Law."

47/ Treaty of Extradition between the United States and Mexico, 31 Stat. 1818. Article III bars proceedings for crimes or offenses of a political character.

The record fails to reveal any effort by respondents -- or anyone else -- to utilize this treaty in reclaiming appellants.

But in the case at bar, the appellants, having been merely paroled from Mexico, are, as we have said, still subjects of Mexico. The latter country has granted them political asylum (R. 4), by virtue of which it has officially undertaken to protect appellants from persecution in Spain. For the United States to violate the terms of the parole would be tantamount to an act of transgression upon the territorial sovereignty of Mexico. 48/

See: United States v. Rauscher, 119 U. S. 407, 419-421.

And for what? The District Court believed it was under a duty to order the return of appellants to their ships in order to maintain "the dignity of the Naval service of foreign nations and [to discourage] desertion by crew

48/ "Oftentimes by process bearing no resemblance to extradition, the fugitive is returned to the country from which he has fled and is sought to be prosecuted criminally. Thus he may be abducted from foreign territory by agents of the State of prosecution. In such event the State whose territory has been invaded may demand the return of the individual."

Hyde, International Law, Chiefly as Interpreted and Applied in the United States, Vol. I, p. 581.

See also: Dickinson, Jurisdiction Following Seizure or Arrest in Violation of International Law, 27 Am. J. Int'l Law, 231, 244 (1933).

Garcia-Mora, International Law and Asylum as a Human Right, p. 153.

The first part of the paper is devoted to the study of the
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$$L(x) = \frac{1}{x} \int_0^x L(t) dt$$
 and to the study of the function $M(x)$ defined by the equation

$$M(x) = \frac{1}{x} \int_0^x M(t) dt$$

The fourth part of the paper is devoted to the study of the
 properties of the function $N(x)$ defined by the equation

$$N(x) = \frac{1}{x} \int_0^x N(t) dt$$
 and to the study of the function $O(x)$ defined by the equation

$$O(x) = \frac{1}{x} \int_0^x O(t) dt$$
 and to the study of the function $P(x)$ defined by the equation

$$P(x) = \frac{1}{x} \int_0^x P(t) dt$$

The fifth part of the paper is devoted to the study of the
 properties of the function $Q(x)$ defined by the equation

$$Q(x) = \frac{1}{x} \int_0^x Q(t) dt$$
 and to the study of the function $R(x)$ defined by the equation

$$R(x) = \frac{1}{x} \int_0^x R(t) dt$$
 and to the study of the function $S(x)$ defined by the equation

$$S(x) = \frac{1}{x} \int_0^x S(t) dt$$

members". 49/ While this is a laudable objective, it can be realized only within the limits permitted by International and Municipal Law.

In the final analysis, however, it was the respondents who chartered the course which now frustrates the exercise of their purported duty. In their haste to serve the interests of a ruthless dictator, the respondents have ignored appellants' plea for asylum; they have misused and abused their statutory authority; and they have disregarded the claims of a more compassionate neighbor. That respondents should have unwittingly left the door to Mexico ajar is all the more fortunate -- for conscience sake.

49/ See Order Denying Petition, etc. (Clk. T. 39).

CONCLUSION

For the foregoing reasons, the Order of the District Court Denying the Petition for a Writ of Habeas Corpus and for Injunction, etc., should be reversed, with directions that said Court make an order for the return of appellants forthwith to Mexico.

Respectfully submitted,

A. L. WIRIN and

HUGH R. MANES

Counsel for Appellants.





A P P E N D I X " A "

Articles appearing in New York Times, 1946-1957, relating to conditions in Spain of which this Court is asked to take judicial notice:

A. FORM OF GOVERNMENT

1. Franco describes his 20 year rule as only way of combating Communism ... 7/9/57 - p. 16, col. 1.
2. Dissatisfaction with government widespread ... 1/21/56 - p. 1, col. 2; 5/31/57 - p. 1, col. 8.
3. Franco life tenure law - June-July, 1947, p. 1951, col. 2.
4. Franco's support of Axis revealed by State Dept. ... 10/8/50 - p. 43, col. 1.
5. Article on nature of Franco rule ... 8/20/50 - VI-p. 13.
6. Franco regime described by Congressmen and others as totalitarian ... 8/2/50 - p. 1, col. 3; 8/15/50 - p. 28, col. 6; 1/10/50 - p. 34, col. 3; 8/30/51 - p. 22, col. 1; 6/4/52 - p. 23, col. 1 (Eisenhower).
7. Political trials denounced ... 4/6/52 - p. 22, col. 3.
8. House Sub-Committee stresses arms aid does not imply approval of government ... 4/11/52 - p. 5, col. 1.

B. CENSORSHIP

1. Government bars two cultural magazines ... 1/28/56 - p. 2, col. 7.
2. Son of Count and printer tried for articles in Monarchist publication critical of Franco ... 7/19/53 - p. 4, col. 6.
3. French newsman expelled for alleged false reporting ... 11/22/53 - p. 13, col. 5.
4. N. Y. Times, and its writer, attacked in Falange newsorgan for critical articles ...

5. 9/24/56 - p. 2, col. 5; 10/2/56 - p. 34, col. 7.
Brother of Spanish writer killed in reprisal
for latter's attacks on regime ... 7/7/47 -
p. 12, col. 3.
6. Attack by Falangists on N. Y. Times photographer
... 3/2/50 - p. 16, col. 1.
7. UNESCO books on Human Rights suppressed ...
10/22/51 - p. 16, col. 3.
8. Credentials of N. Y. Times correspondent re-
voked ... 4/18/52 - p. 24, col. 5. (Later re-
accredited.)
9. Suppression of book offering gradual restora-
tion of liberties under Constitutional Monarchy
... 11/23/52 - p. 25, col. 1.
10. Issues of N. Y. Times banned ... 11/21/52 -
p. 7, col. 4; 11/28/52 - p. 15, col. 2.
11. Two religious magazines suppressed ... effort
to curb separatism ... 7/8/52 - p. 30, col. 3;
7/9/52 - p. 22, col. 2; 7/12/52 - p. 32, col. 6.

C. SUPPRESSION OF POLITICAL ORGANIZATION
- AND OF FREEDOM OF ASSOCIATION

1. Groups of alleged Communists held for political
activity ... 5/14/57 - p. 4, col. 6.
2. Suppression by terror of pro-Monarchist and
Christian Democratic groups ... 5/29/57 - p. 3,
col. 4.
3. Arrest of alleged anarchists - top labor leaders
on trial ... 1/8/53 - p. 14, col. 1.
4. Thirty-eight youths sentenced for organizing
political party ... 3/19/53 - p. 10, col. 6.
5. Twelve members of clandestine Socialist
Party seized in raids on meeting, one dies
in jail ... 2/22/53 - p. 9, col. 2; 2/27/53 -
p. 3, col. 5.
6. Eleven Socialists jailed for forming illegal
party ... 11/26/53 - p. 14, col. 3.
7. Twenty-one convicted, and terms enlarged,
for organizing Masonic Lodge, regarded as
subversive ... 7/16/55 - p. 16, col. 7.
8. Thirty held for trying to organize Catalonian
Communist Party ... 7/22/53 p. 13, col. 3.
9. Death sentence asked for men accused of main-
taining relations with exiles ... 10/26/47 -
p. 39, col. 4.

1. The first part of the book is devoted to a general survey of the history of the subject.	1
2. The second part is devoted to a detailed examination of the various theories of the subject.	2
3. The third part is devoted to a critical examination of the various theories of the subject.	3
4. The fourth part is devoted to a critical examination of the various theories of the subject.	4
5. The fifth part is devoted to a critical examination of the various theories of the subject.	5
6. The sixth part is devoted to a critical examination of the various theories of the subject.	6
7. The seventh part is devoted to a critical examination of the various theories of the subject.	7
8. The eighth part is devoted to a critical examination of the various theories of the subject.	8
9. The ninth part is devoted to a critical examination of the various theories of the subject.	9
10. The tenth part is devoted to a critical examination of the various theories of the subject.	10

11. The eleventh part is devoted to a critical examination of the various theories of the subject.	11
12. The twelfth part is devoted to a critical examination of the various theories of the subject.	12
13. The thirteenth part is devoted to a critical examination of the various theories of the subject.	13
14. The fourteenth part is devoted to a critical examination of the various theories of the subject.	14
15. The fifteenth part is devoted to a critical examination of the various theories of the subject.	15
16. The sixteenth part is devoted to a critical examination of the various theories of the subject.	16
17. The seventeenth part is devoted to a critical examination of the various theories of the subject.	17
18. The eighteenth part is devoted to a critical examination of the various theories of the subject.	18
19. The nineteenth part is devoted to a critical examination of the various theories of the subject.	19
20. The twentieth part is devoted to a critical examination of the various theories of the subject.	20

10. Government wars on underground press ... 8/24/47 - VI - p. 37, col. 2.
11. Twenty-four sentenced for Socialist Party membership ... 2/1/49 - p. 17, col. 1; others - 2/8/49 - p. 14, col. 6.
12. Official Falange paper, Arribe, charges Protestant Church backed by foreign aid funds, hints at disloyalty ... 4/22/50 - p. 3, col. 1; 7/19/50 - p. 2, col. 5.
13. Arrests of Monarchists ... 3/1/50 - p. 17, col. 1; 3/10/50 - p. 5, col. 5; 3/12/50 - p. 11, col. 1.
14. Military trial of twenty-seven for attempt to organize Socialist Party groups ... 7/3/52 - p. 6, col. 8; 7/4/52 - p. 5, col. 4; 7/5/50 - p. 2, col. 7; 7/8/52 - p. 12, col. 5.
15. Several members of Workers Party arrested ... 5/21/52 - p. 11, col. 2.

D. MAINTENANCE OF POWER BY FORCE AND TERROR

1. Disappearance of prominent anti-Franco exile ... 4/11/57 - p. 15, col. 1.
2. Students clash with police over cost of living protest ... 2/9/57 - p. 1, col. 8.
3. Student pickets attacked by Falangists ... 2/9/56 - p. 9, col. 3.
4. Nine executed for political activities ... 3/9/52 - p. 26, col. 3; five more - 3/13/52 - p. 10, col. 3; and five more - 3/15/52 - p. 4, col. 6.
5. Fourteen executions reported ... 8/29/47 - p. 10, col. 7.
6. Eighteen tried in Acoma for revolt ... 3/25/50 - p. 1, col. 2.
7. Four executed for "terrorism" ... 2/18/49 - p. 19, col. 4. See also: 2/22/49 - p. 7, col. 4.

E. SUPPRESSION OF SPEECH

1. Arrest of prominent anti-Franco leaders for "subversion" ... 7/1/57 - p. 2, col. 7.
2. Man held for remarks injurious to State ... 4/17/57 - p. 5, col. 1.

1. The first part of the book is devoted to a general introduction to the subject of the book.	1
2. The second part of the book is devoted to a detailed description of the various methods of the subject.	15
3. The third part of the book is devoted to a detailed description of the various methods of the subject.	25
4. The fourth part of the book is devoted to a detailed description of the various methods of the subject.	35
5. The fifth part of the book is devoted to a detailed description of the various methods of the subject.	45
6. The sixth part of the book is devoted to a detailed description of the various methods of the subject.	55
7. The seventh part of the book is devoted to a detailed description of the various methods of the subject.	65
8. The eighth part of the book is devoted to a detailed description of the various methods of the subject.	75
9. The ninth part of the book is devoted to a detailed description of the various methods of the subject.	85
10. The tenth part of the book is devoted to a detailed description of the various methods of the subject.	95

APPENDIX I. THE FIRST PART OF THE BOOK IS DEVOTED TO A GENERAL INTRODUCTION TO THE SUBJECT OF THE BOOK.

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9. The ninth part of the book is devoted to a detailed description of the various methods of the subject.	85
10. The tenth part of the book is devoted to a detailed description of the various methods of the subject.	95

APPENDIX II. THE SECOND PART OF THE BOOK IS DEVOTED TO A DETAILED DESCRIPTION OF THE VARIOUS METHODS OF THE SUBJECT.

1. The first part of the book is devoted to a general introduction to the subject of the book.	1
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10. The tenth part of the book is devoted to a detailed description of the various methods of the subject.	95

3. Thirty-three described as Communists as security threats ... 4/12/57 - p. 8, col. 4.
4. American bull fighter Whitney gets six year jail term for "insulting nation" ... 7/9/56 - p. 17, col. 2. (Later pardoned.)
5. Two tried by Military Court for conspiracy against Franco ... 2/10/53 - p. 4, col. 2.
6. U. S. tourist tried after being held 2-1/2 months for public criticism of Franco regime ... 5/26/55 - p. 8, col. 6.
7. Six Anarchists held for publishing anti-government bulletin ... 7/13/55 - p. 4, col. 8.
8. Ten Socialists sentenced to up to 15 years for anti-Franco acts ... 2/13/54 - p. 3, col. 7.
9. Student demonstration protesting cost of living broken up by police ... 2/8/57 - p. 6, col. 4.
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11. Executioning of alleged Communists notwithstanding intervention of Pope ... 12/20/47 - p. 3, col. 1.
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SUPPRESSION OF CIVIL RIGHTS AND LIBERTIES

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4. Government suspends right to move place of residence and protections against unlawful arrest in move to curb student rioting ... 2/11/56 - p. 1, col. 2.
5. Death penalty for plotting sabotage ... 5/7/47 - p. 11, col. 2.
6. Anti-Franco labor organizations labelled anarchist - leaders imprisoned 18 months without trial ... 2/6/54 - p. 4, col. 3.

7. Government announces 33,835 political prisoners - opponents say figure too low ... 7/9/50 - p.32, col.3.
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9. Government reveals political prisoners at 31,000 ... 10/25/51 - p.12, col.4.
10. Franco conditionally frees 113 ... 8/21/52 - p.7, col.5. Another 400 ... 8/28/51 - p.5, col.2.
11. Sulzberger reports most Franco foes classed as Communists - attacks violation of civil rights ... 11/30/48 - p.12, col.3.

G. POVERTY, INFLATION AND SUPPRESSION OF STRIKES AND PROTEST

1. Disappointment of youth with economic conditions noted ... 1/6/56 - p.4, col.3.
2. Execution of five trade unionists denounced ... 5/16/52 - p.9, col.1.
3. Sedition trial arising out of strikes ... 3/17/54 - p.3, col.3; 3/27/54 - p.4, col.3.
4. 2000 shipyard workers fired for striking against overtime pay cut - labor unrest reported ... 12/10/53 - p.1, col.7.
5. Report shows 83% of people account for one-third national income ... 7/7/53 - p.18, col.2.
6. Strike wave as prices rise ... 5/27/56 - IV - p.4, col.5.
7. Inflation rampant - 1/13/57 - p.36, col.1.
8. Cost of living up 25% in one year ... 1/28/57 - p.31, col.7.
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H. PLIGHT OF POLITICAL REFUGEES

1. Amnesty law said to exclude Franco foes and political prisoners ... 8/3/47 - p.32, col.3.
2. Charge Lt. Col. Beneyto Sopena executed after return under amnesty offer ... 12/30/56 - IV - p.6, col.6.

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3. Exiles' failure to take advantage of suspension of penalties for illegal entry cited ... 12/26/49 - p. 2, col. 7.

I. SEE ALSO: "THE ENCYCLOPEDIA AMERICANA, VOL. 12., ...

... wherein Franco is said to have declared after the Civil War that he was "responsible only to God and history".

J. SEE ALSO: "UNIVERSAL WORLD REFERENCE ENCYCLOPEDIA" ...

... depicting the career and some of the activities of Franco since 1939, as follows:

"Franco made himself the head of a totalitarian Government. He was also premier, commander-in-chief of the armed forces, and head of the only political party allowed to function, the FALANGE PARTY. In World War II Franco gave all aid to Germany short of going to war."

K. SEE ALSO: H. L. MATTHEWS, "THE YOKE AND THE ARROW".

* * *



That the record at bar casts appellants in the role of political refugees, is dramatically revealed in these excerpts from their uncontroverted testimony:

MANUEL RODRIGUEZ:

"[I left the ship] in order to ask political help [in Mexico]" (R. 9).

"I was fleeing the Franco regime (R. 15) Because I am not in agreement with the regime or with the Laws of Spain and because I want a free country . . . and in Spain, there is no freedom to live for the man or his way of living" (R. 16).

"Two [of my] brothers . . . died [in the Civil War] and one that is still alive . . . [is] in Chile . . . [because] fleeing from Spain, from Franco, from the regime" (R. 16, 17).

"They made me join [The Falange] against my will . . . " (R. 18).

"[I quit] because I wasn't in agreement with the principles of the Falange, and because they were the ones who killed my brother" (R. 18).

" . . . I had to defend [Franco] and also to comply with all the Laws of Franco; and because if I did not do that, I would not be able to work . . . because I did not want to go to the classes of the Falange . . . they fired me" (R. 19).

"As soon as the Franco regime came in, all the Spaniards who were left that belonged to the other side were put in jail and were shot.

Then the people who were not willingly going to see those people being shot were called 'Reds' and they were beaten and they were also at times killed. These I have seen myself, with my father and my brothers" (R. 22, 23).

" . . . a few of us, the sailors, we talked about it and decided we wanted a free country . . . and then we would go away, we would escape" (R. 35).

GINAS JIMINEZ NORTES (MARTINEZ):

"Why did I go? Because I was fleeing from the regime of Franco" (R. 44).

" . . . we had no freedom [in Spain] and I was looking for a country where I could be free and I could do whatever my capacity and my reasoning decided for me" (R. 45).

" . . . when I went into the Institute [University] they made me enter the Falange, not because I wanted to but because of force" (R. 45).

" . . . I renounced the Falange, because I could not stand the regime that Franco gave us" (R. 46).

"[We had to take] an oath to support Franco, and . . . I did not want to give anything, because he did not give us freedom" (R. 47).

"During the War, my father didn't want to fight on Franco's side, so he was persecuted and they put him in jail several times" (R. 48).

"I do not know of any [other instances of political activity in Spain], because they do not allow us to speak of those things, and if they catch one of us they will put you in jail for four to six years" (R. 48-49).

"I wasn't thinking of deserting. I was thinking of leaving the Franco regime and go to a free country where a man could use his freedom" (R. 50).

" . . . I joined the Navy in Spain, because I understood that I could not work there and I wanted to live in a free country" (R. 53).

" . . . I went into [the Navy] as an office worker . . . but then in no time, saying I did not want the Franco regime, I was against it, I lost that job and then they gave me lower types of work" (R. 54).

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CHAPTER IV

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" . . . A man who is not free always looks for a country where he can be free . . . " (R. 54).

"[If I am returned to Spain] the least I would get would be at least six years in jail, that is, if they would not shoot me, because on top of all the things we have said about [Franco] here which he deserves . . . so if I were to return to Spain now the most sure thing that they would do would be shoot me, because they would not be satisfied after my having said what I have said . . . " (R. 55).

ENRIQUE MEDINA FERNANDEZ:

" . . . I wanted to go to Mexico (R. 59) . . . because I was looking for a free country where they would respect the rights of a citizen and where you could earn money and have the means to live as such, because in Spain a workman works very hard and he doesn't get enough money to live . . . " (R. 61).

"Because of the fear that I have of returning to Spain of the things that we have said in Mexico . . . and the things we think, I would have a fear" (R. 61).

"A fear that they would put us in jail or that they would kill us because of having spoken against the government" (R. 62).

THE UNIVERSITY OF CHICAGO
CHICAGO, ILLINOIS

TO THE PRESIDENT OF THE UNIVERSITY OF CHICAGO
AND THE FACULTY OF THE DIVISION OF THE PHYSICAL SCIENCES
I have the honor to acknowledge the receipt of your letter of the 10th inst.
and in reply to inform you that the same has been forwarded to the
proper authorities for their consideration. I am, Sir, very respectfully,
Yours, very truly,
J. H. VAN VLIET

RECEIVED JAN 11 1907

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